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No. 05-

IN THE

Supreme Court of the United States

MCLANE WESTERN, INC.,
Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF COLORADO, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the Colorado Court of Appeals, Division IV

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Does a state tax on activities related to the distribution of a product in the State, which increases because more stages in the distribution chain are located outside the State rather than within the State, impermissibly discriminate against interstate commerce?

PARTIES TO THE PROCEEDING

In addition to the parties listed in the caption, respondents include M. Michael Cooke, sued in her official capacity as the Executive Director of the Department of Revenue of the State of Colorado.

Fred Fisher, former Executive Director of the Department of Revenue of the State of Colorado, was sued in his official capacity in petitioner's initial complaints, but was substituted upon retirement prior to the judgments below.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

McLane Western, Inc. is a wholly-owned subsidiary of McLane Company, Inc. McLane Company, Inc. is a wholly-owned subsidiary of Berkshire Hathaway Inc., a publicly-traded company. McLane Western, Inc. has no subsidiaries.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner McLane Western, Inc. ("McLane") respectfully petitions for a writ of certiorari to review the judgment of the Colorado Court of Appeals, Division IV, in this case.

OPINIONS BELOW

The opinion of the Colorado Court of Appeals (App., *infra*, 1a-13a) is reported at 126 P.3d 211. The opinions and orders of the District Court, City and County of Denver, Colorado, entering summary judgment for respondents (App., *infra*, 14a-24a) and denying McLane's motion to alter or amend judgment (*id.* at 25a) are not officially reported. The Colorado Supreme Court's denial of McLane's petition for a writ of certiorari (*id.* at 26a-27a) is not officially reported.

JURISDICTION

The judgment of the Colorado Court of Appeals was entered on May 5, 2005. *Id.* at 1a-13a. The Colorado Supreme Court denied McLane's petition for a writ of certiorari on January 9, 2006. *Id.* at 26a-27a. The jurisdiction of this Court rests on 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Commerce Clause of the United States Constitution, U.S. Const., art. I, § 8, cl. 3, provides, in relevant part: "The Congress shall have Power * * * [t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes."

Relevant portions of the Colorado statutes, Colo. Rev. Stat. §§ 39-28.5-101 and 39-28.5-102 (1986), are set forth at App., *infra*, 28a-29a.

STATEMENT OF THE CASE

This case involves the constitutionality of a Colorado excise tax on activities related to the distribution of tobacco products in the State. The State imposes the tax on the initial distribution activity that occurs in Colorado. The tax base is the price paid for the product by the distributor who "first receives" (Colo. Rev. Stat. § 39-28.5-101(2)) the product in Colorado (the "first Colorado distributor"). A tax rate of 20 percent was applied to this base during the relevant time period. Because the price of the product increases as it moves through the distribution network, which includes manufacturing, packaging, transportation, and marketing, the tax base is necessarily lower when all the steps in the distribution network are performed by entities located within the State. By the same token, the tax base is necessarily higher when more steps in the distribution network are performed by entities located outside the State because the price paid by the first Colorado distributor will include the mark-ups reflecting the out-of-state distribution activities.

The court below recognized that "the tax base will be higher the later in the distribution network the product is taxed" (App., *infra*, 6a), and that the determination of the tax base therefore may place petitioner "at a competitive disadvantage in the marketplace[.]" *Id.* at 8a. But the court rejected the claim that an increase in the tax base attributable to the out-of-state location of more steps in the distribution chain violated the Commerce Clause, because it believed that none of this Court's precedents "involves a determination that a state tax violates the Commerce Clause based on the inequities of a shifting tax base." *Id.* at 10a.

The far-reaching question raised by this case is whether Colorado's taxing regime, whose "shifting tax base" rewards the location of economic activity in Colorado and penalizes the location of economic activity in other States, discriminates against interstate commerce in violation of the Commerce Clause.

1. Factual Background

a. Colorado imposes an excise tax on "the sale, use, consumption, handling, or distribution" in the State of all tobacco products other than cigarettes. Colo. Rev. Stat. § 39-28.5-102(1). The tax is imposed upon the first taxable event that occurs in Colorado. The tax is collected from the first Colorado distributor, *i.e.*, the person in the distribution chain who "first receives" (Colo. Rev. Stat. § 39-28.5-101(2)) the product in Colorado when the first taxable event occurs.[1] *Ibid.*; Colo. Rev. Stat. § 39-28.5-102.

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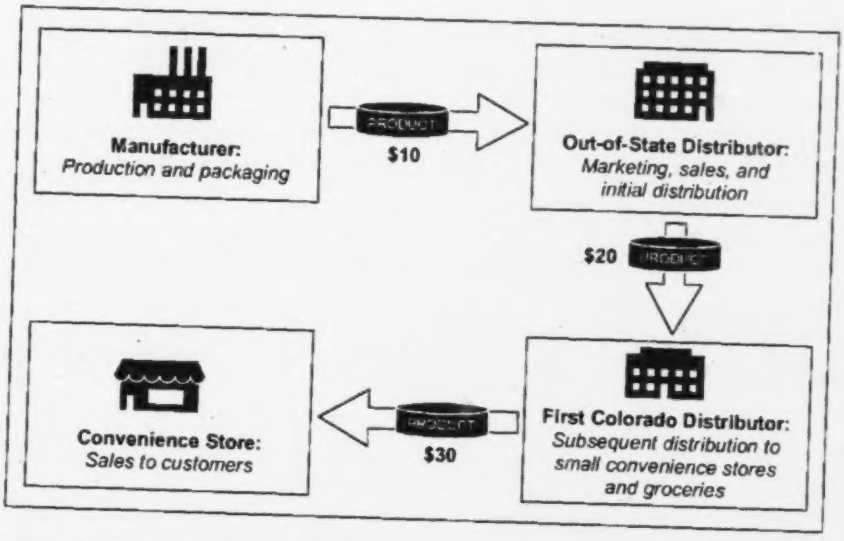
[1] The statute provides alternative events that may identify the first Colorado distributor (and therefore the tax base), including where there is in-state manufacturing or where an in-state retailer receives product from outside the State. Colo. Rev. Stat. § 39-28.5-102(1)(a)-(c). To the extent these alternatives are relevant to this case, they reinforce the discrimination against interstate commerce since they all involve the first in-state

During the time at issue in this case, the tax was imposed at the rate of 20 percent—it has since increased to 40 percent[2]—of the price paid by the first Colorado distributor for the product regardless of the point in the distribution chain at which the first Colorado distributor receives the product. Thus, where significant parts of the chain, *i.e.*, manufacturing, packaging, transportation, and marketing, take place outside the State, the tax is imposed on a price that is much greater than when the entire chain of distribution activity occurs within the State, because in the former situation the price reflects mark-ups at the various steps in the distribution chain whereas in the latter it does not. The base on which the tax is imposed in the latter situation is much lower because that base is the price paid at the first step in the distribution chain following manufacture and before mark-ups that occur further down the chain.

The distribution chain and the increasing tax base may be illustrated as follows:



activity of the distribution chain, regardless of how much the price of the product may have been marked-up outside the State. *Ibid.*

[2] Colo. Rev. Stat. § 39-28.5-102.5 (2005) (additional 20 percent tax levy).

b. Petitioner McLane buys, resells, and ships grocery products from large suppliers to smaller retailers throughout the western United States, including Colorado. App., *infra*, 1a-2a, 15a-16a. Among the products McLane buys and resells are smokeless tobacco products that are subject to the Colorado excise tax. During tax periods spanning March 1990 to December 2001, McLane bought these products from a distributor located outside of Colorado. *Id.* at 2a, 16a-18a. The out-of-state distributor shipped the products by common carrier to McLane's warehouse in Colorado. *Id.* at 2a, 17a-18a. During that time period, McLane paid its out-of-state supplier approximately $95 million for such products. *Id.* at 17a. McLane inspected and accepted or rejected the products at its Colorado warehouse and then resold the products in Colorado to its customers, primarily grocery and small convenience stores. *Id.* at 1a-2a, 16a-18a. Because McLane was the first in-state recipient of the products, *i.e.*, the first Colorado distributor, it was liable for payment of the excise tax.

During the tax periods at issue, McLane paid excise taxes to Colorado of approximately $19 million—20 percent of the $95 million that it paid for the products. *Id.* at 17a. McLane subsequently determined that Commerce Clause considerations (and a proper reading of the state statute) compelled the conclusion that the proper base for the excise tax was the price of the product at the beginning of the distribution network (approximately $42.5 million) rather than the $95 million marked-up price it had paid at the end of the distribution network. Accordingly, McLane recalculated the proper tax due as 20 percent of the lower base of $42.5 million, or approximately $8.5 million. After accounting for a small vendor deduction, McLane filed refund claims with the Colorado Department of Revenue for approximately $10 million (plus statutory interest), which reflects the difference between the $19 million paid and the $8.5 million that should have been paid. *Id.* at 3a, 17a-18a. McLane's refund claims

explicitly rested on the ground, among others, that the use of the marked-up price as the base to determine its excise tax liability discriminated against interstate commerce in violation of the Commerce Clause. The Department denied McLane's refund claims. *Id.* at 3a, 18a.

2. The Proceedings Below

McLane filed suit in the District Court, City and County of Denver, Colorado, against the Department of Revenue for refund of the excise taxes and statutory interest. McLane alleged, among other things, that the use of an excise tax base measured by the marked-up price McLane paid for the products—rather than their lower price at the beginning of the distribution network—discriminated against interstate commerce in violation of the Commerce Clause, because it disadvantages businesses whose distribution chains include significant steps outside of Colorado as compared to businesses whose entire distribution chain is located within the State.

The district court entered summary judgment for the Department. *Id.* at 14a-24a. The court rejected McLane's argument that a proper construction of the state statute required that the base for the tax be measured by the price of the product at the beginning of the distribution network. The court also dismissed McLane's Commerce Clause objections to this interpretation of the statute (*id.* at 23a-24a), but did so based on its view that "[t]he tax base for McLane would be the same" regardless of where business was done (*id.* at 24a), a view later rejected by the court of appeals. *Id.* at 6a.

The court of appeals affirmed. *Id.* at 1a-13a. The court rejected the district court's view that McLane's tax base would be the same regardless of how much of the distribution network was located in Colorado (*id.* at 6a) and, instead, expressly recognized that the excise tax creates a "shifting tax base." *Id.* at 10a. The court nevertheless agreed with the district court that the statute required that McLane pay the tax

based on the marked-up price it paid for the product. *Id.* at 6a, 8a, 12a-13a. Consequently, the court of appeals squarely confronted the fundamental constitutional question raised by this case:

> Whether a tax on a "shifting tax base" (*id.* at 10a)—namely, a tax base that will "be at its lowest level" when "the manufacturers, suppliers, or distributors involved in the product's distribution network" are "located within Colorado" (*id.* at 6a)—discriminates against interstate commerce in violation of the Commerce Clause.

The court recognized that this Court's Commerce Clause jurisprudence condemns as unconstitutionally discriminatory a levy that either "taxes out-of-state transactions or entities at a rate higher than it taxes in-state transactions, entities, or products," or "exempts in-state transactions, entities, or products from an otherwise uniform tax." *Id.* at 7a. In the court's view, however, any discrimination that falls outside the precise confines of these specific prohibitions is not cognizable under the Commerce Clause.

The court acknowledged that "the location of the manufacturers, suppliers, or distributors involved in the product's distribution network and the price mark-up of each impacts the tax base or the price upon which the constant twenty percent tax rate is imposed." *Id.* at 6a. Even more to the point, the court acknowledged that "if the manufacturer and all the distributors were located within Colorado, the tax base would be at its lowest." *Ibid.* Nonetheless, the demands of the Commerce Clause were satisfied, according to the court, as long as "[a]ll taxable distributors * * * are taxed at the same rate and on a tax base determined in the same fashion." *Id.* at 8a. The court was unfazed by the discrimination that lies at the heart of this case—the discrimination created by a shifting base on which the tax is imposed—because of the purported lack of a precedent involving "a determination that a state tax violates the Commerce Clause based on the inequities of a

shifting tax base." *Id.* at 10a. Thus, even though the Colorado excise tax imposes a higher tax when more steps in the distribution process occur outside the State, and even though (as the court conceded) this "may place the product at a competitive disadvantage in the marketplace because the higher tax is added to the price" (*id.* at 8a), this was insufficient in the court's view to "render the tax unconstitutional under the Commerce Clause." *Ibid.*

The Colorado Supreme Court denied McLane's petition for a writ of certiorari. *Id.* at 26a-27a.

REASONS FOR GRANTING THE PETITION

The decision of the Colorado Court of Appeals warrants review by this Court for two compelling reasons. First, the court of appeals' determination that the Commerce Clause is not violated by an excise tax that increases when more links in a distribution chain are located outside the State and is at its lowest when all the links in the chain are located within the State is in profound tension with this Court's precedents barring discrimination against interstate commerce "whether forthright or ingenious." *Best & Co. v. Maxwell*, 311 U.S. 454, 455 (1940). By sustaining a tax that admittedly creates "a competitive disadvantage in the marketplace" (App., *infra*, 8a) when a product's distribution network lies outside the State, the court throws into question bedrock Commerce Clause doctrine barring discrimination against products and activities that cross state lines.

Second, the Colorado Court of Appeals' decision, if allowed to stand, would provide a template for States to discriminate against interstate commerce by the simple expedient of effectuating such discrimination through a shifting tax base rather than through the more forthright forms of discrimination that courts routinely condemn as unconstitutionally discriminatory under the Commerce Clause. For example, tax exemptions or credits for in-state products—

quintessential violations of settled dormant Commerce Clause doctrine (*see, e.g., Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984) (exemption); *New Energy Co. v. Limbach*, 486 U.S. 269 (1988) (credit))—would pass muster if reconfigured as unobjectionable "inequities of a shifting tax base." App., *infra*, 10a. A "tax base" exception to the Court's prohibition against discriminatory state taxation would therefore open a gaping hole in the constitutional structure that protects interstate commerce from unconstitutionally burdensome state taxes. The extraordinary implications of such a rule require review by this Court.

I. THE STATE COURT'S APPROVAL OF A STATE EXCISE TAX THAT IS GREATER WHEN MORE STEPS IN A DISTRIBUTION CHAIN OCCUR OUTSIDE THE STATE CONFLICTS WITH THIS COURT'S COMMERCE CLAUSE JURISPRUDENCE

"Time and again this Court has held that, in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate 'differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter.'" *Granholm v. Heald*, 125 S. Ct. 1885, 1895 (2005) (quoting *Oregon Waste Sys., Inc. v. Department of Envtl. Quality*, 511 U.S. 93, 99 (1994)). Taxes discriminating against interstate commerce fall squarely within this prohibition. *See, e.g., South Cent. Bell Tel. Co. v. Alabama*, 526 U.S. 160 (1999); *Fulton Corp. v. Faulkner*, 516 U.S. 325 (1996). And so does Colorado's tobacco excise tax.

The disparate treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter is undisputed in this case. The tax at issue was measured by the marked-up price McLane paid when it received the product in the State as the first Colorado distributor. The tax would have been substantially less if "the manufacturers,

suppliers, or distributors involved in the product's distribution network" had been "located within Colorado," because the tax would apply before the price mark-ups occurred, and "the tax base would be at its lowest level." App., *infra*, 6a. For the same reason, when the distribution network is located outside of Colorado, as in the instant case, the tax will be greater, because the tax applies after the mark-ups reflecting out-of-state activity occur. Simply put, as the court below recognized, "the tax base will be higher the later in the distribution network the product is taxed[.]" *Ibid.* The lower tax borne by the product when the distribution network is entirely in Colorado, and the higher tax borne by the product when the distribution network is outside Colorado, inescapably constitutes the "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter" that violates the Commerce Clause. *Granholm*, 125 S. Ct. at 1895.

The contrary ruling by the Colorado Court of Appeals warrants review because it conflicts with well-established precedent of this Court.

A. The Ruling Below Is Contrary To *Halliburton*

In *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), this Court struck down a state tax on the ground that a shifting tax base, analogous to the Colorado tax base at issue here, discriminated against interstate commerce in violation of the Commerce Clause. *Halliburton* involved Louisiana's sales and use tax regime, whose purpose was "to make all tangible property used or consumed in the State subject to a uniform tax burden irrespective of whether it is acquired within the State, making it subject to the sales tax, or from without the State, making it subject to a use tax at the same rate." *Id.* at 66. The tax base of Louisiana's sales and use tax regime was the "sales price" of items sold in the State

and the "cost price" of articles sold outside the State, but used within the State.

The State defined the "cost price" tax base, however, as the actual cost of the articles brought into the State without any deduction for labor. Therefore, when the taxpayer, after acquiring materials in Oklahoma and assembling them there into specialized equipment, brought the assembled equipment into Louisiana for use in its business of servicing oil wells, Louisiana assessed a two percent use tax on the "cost price" tax base of the equipment. The "cost price" tax base was the purchase price of the materials plus the value added in Oklahoma by the taxpayer's labor in assembling the equipment. By contrast, if the taxpayer had acquired the materials in Louisiana and assembled them there, it would have paid a two percent sales tax on the "sales price" tax base of the equipment, but would not have paid a tax on its labor costs.

The Court struck down the tax on the ground that the shifting tax base discriminated against interstate commerce. Although the rate of tax was the same regardless of where the taxpayer assembled or used its equipment, the differential treatment that burdened the out-of-state economic interests and benefited the in-state interests was apparent. The Court observed that the out-of-state manufacturer's "*tax base* is *increased* through the inclusion of its product's labor and shop overhead," because it had occurred out of State, *id.* at 70 (emphasis added), and that *increase* in the tax base attributable to out-of-state activity was a source of discrimination that led the Court to invalidate the tax because of the "resulting tax inequality." *Id.* at 71.

The analogy between *Halliburton* and the instant case could hardly be closer. In both cases, the state statute imposed a tax on various related taxable events (sale, use, *etc.*). In both cases, the tax was imposed on the first taxable event that occurred within the State. In both cases, the measure of the tax was the price of tangible personal property. And in both

cases, the tax base increased as more economic activity occurred outside the State and decreased as more economic activity occurred inside the State.

Thus, in *Halliburton*, the tax base increased because assembly activity occurred outside Louisiana, just as in the instant case the tax base increases because distribution activity occurs outside Colorado. Similarly, in *Halliburton*, the tax base decreased when assembly activity occurred in Louisiana, just as in the instant case the tax base decreases when distribution activity occurs in Colorado. In both cases, the source of the unconstitutional discrimination is the increase in the tax base attributable to the mark-up of the property's price to reflect the out-of-state activity. When that out-of-state activity occurs in the State, the tax base is lower because the tax is triggered at an earlier point in the distribution process, before the value-adding activities reflected in the marked-up price of the property have occurred. As a matter of substance, *Halliburton* and the instant case are identical twins, and if one of them is good law the other cannot be.

Halliburton remains bedrock Commerce Clause doctrine. *Granholm*, 125 S. Ct. at 1897 (citing *Halliburton*); *Fulton*, 516 U.S. at 333 n.3 (same); *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 192 n.6 (1995) (same); *Associated Indus. of Mo. v. Lohman*, 511 U.S. 641, 648 (1994) (same); *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Fin.*, 505 U.S. 71, 78 (1992) (same); *Trinova Corp. v. Michigan Dep't of Treasury*, 498 U.S. 358, 385 (1991) (same). For example, in *Amerada Hess Corp. v. Director, Division of Taxation*, 490 U.S. 66 (1989), the Court reiterated the fundamental proposition that States may not create taxing regimes that induce businesses to ply their trade within a State rather than in interstate commerce, and cited *Halliburton*, observing that the "Louisiana statute had the discriminatory effect of imposing a greater tax on the same

goods if they were manufactured outside Louisiana than if they were manufactured within the State, thereby creating an incentive to locate the manufacturing process within the State." *Id.* at 76. The same point applies here with respect to the location of the distribution chain in Colorado. *See also Fulton*, 516 U.S. at 327 (invalidating as unconstitutionally discriminatory under the Commerce Clause a state intangible property tax on corporate stock that varied inversely with the corporation's economic activity in the State); *Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388, 401 (1984) (invalidating as unconstitutionally discriminatory a tax credit scheme that "penalizes increases in * * * activities in other States").

The State of Colorado is not, of course, left without a means of imposing an evenhanded excise tax. Constitutionally permissible excise taxes are imposed on a tax base that does not change depending on whether economic activity occurs within or without the State. For example, a constitutional excise tax may be imposed on the number of units of a product brought into the State, such as gallons of gasoline. Colo. Rev. Stat. § 39-27-102(1)(a)(II)(A) (levying gasoline tax of 20 cents per gallon). Similarly, there can be no constitutional objection to an excise tax imposed on the value of a product at a particular point in the distribution chain (manufacture, wholesale, or retail) as long as the point in the chain at which the tax is imposed does not vary depending upon whether the distribution chain itself is located within the State. Colo. Rev. Stat. § 39-26-104(1)(a) (levying sales tax on retail sales price).

B. The Court Of Appeals' Cramped Reading Of This Court's Commerce Clause Precedent Should Not Be Allowed To Stand

The Colorado Court of Appeals' dismissal of McLane's Commerce Clause claim for want of a controlling "shifting tax base" precedent was misguided for two reasons. First, as

we have already demonstrated, there *is* such a precedent on point, namely *Halliburton*. Second, the state tax discrimination here offends core Commerce Clause principles.

Significantly, the court of appeals did not contest the underlying Commerce Clause logic of petitioner's argument, namely, that the State's tax base increased when more of the distribution chain was located outside of Colorado and decreased as more of the distribution chain was located in Colorado. To the contrary, the court embraced it. Thus the court explicitly conceded that "the tax base calculated on the price paid by the taxable distributor may place the product [from outside the State] at a competitive disadvantage in the marketplace because the higher tax is added to the price[.]" App., *infra*, 8a. What led the court of appeals to uphold this "competitive disadvantage" against constitutional challenge was not a failure of logic, but rather the purported absence of a precedent on point.

But this Court has made clear in one way or another on countless occasions that the Commerce Clause forbids state tax discrimination regardless of the form that it takes or the statutory mechanism that produces it. The Court has declared that "[a]ctual discrimination, wherever it is found, is impermissible." *Associated Indus.*, 511 U.S. at 650. The Court has expressly "declined to attach any constitutional significance to * * * formal distinctions that lack economic substance" in evaluating claims of state tax discrimination. *Westinghouse*, 466 U.S. at 405. It has long been established that "'[t]he commerce clause forbids discrimination, whether forthright or ingenious. In each case it is our duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against interstate commerce.'" *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 201 (1994) (quoting *Best*, 311 U.S. at 455-456). In short, a state tax regime favoring in-state over out-of-state economic interests violates the Commerce Clause

regardless of whether the source of the discrimination lies in the rate, an exemption, a credit, or the base.

The court of appeals' failure to reconcile its decision with *Halliburton*, its focus on the form rather than the substance of the discrimination at issue here, and its unwarranted reliance on a purported "shifting tax base" exception to the non-discrimination principle of the dormant Commerce Clause in the face of a tax regime that admittedly creates a "competitive disadvantage" for products that cross state lines (App., *infra*, 6a, 8a, 10a), underscore the need for this Court's review. Left unreviewed, the court's cramped analysis stands as precedent that unduly narrows this Court's Commerce Clause jurisprudence and ignores the fact that the prohibition against state tax discrimination requires an analysis of the practical effect of the challenged scheme.[3]

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[3] This Court currently is considering in *DaimlerChrysler Corp. v. Cuno*, 386 F.3d 738 (6th Cir. 2004), *cert. granted*, 126 S. Ct. 36 (2005) (No. 04-1704), and *Wilkins v. Cuno*, 386 F.3d 738 (6th Cir. 2004), *cert. granted*, 126 S. Ct. 36 (2005) (No. 04-1724), a challenge to a tax incentive that allegedly violates the Commerce Clause by rewarding a taxpayer for locating activities within the State. Regardless of how the Court resolves the questions in those cases, which include standing as well as substantive Commerce Clause issues, this case is distinguishable in two essential respects: first, petitioner clearly has been harmed by the Colorado tax (with more than $10 million of tax liability in dispute); second, there clearly is a burden on interstate commerce because the tax increases when more steps in the distribution chain are located outside, rather than within, the taxing State.

II. IF LEFT UNREVIEWED, THE DECISION BELOW WILL SERIOUSLY UNDERMINE COMMERCE CLAUSE RESTRAINTS ON DISCRIMINATORY STATE TAXES IN CONTEXTS WELL BEYOND THE FACTS OF THIS PARTICULAR CASE

The flawed ruling by the Colorado Court of Appeals has extraordinary practical implications. If left unreviewed, the court of appeals' decision will provide a simple formula for state legislatures to enact discriminatory state taxes that will be immune from challenge and will thereby seriously undermine long-standing Commerce Clause restraints on taxes favoring in-state over out-of-state economic interests.

A. The Ruling Below Would Allow State Taxing Authorities Easily To Transform Otherwise Unconstitutional Taxes Into Permissible Tax Schemes That Discriminate Against Interstate Commerce

The practical implications of leaving undisturbed the court of appeals' decision are considerable. First, it is a fairly easy task to transform a tax that unconstitutionally discriminates against interstate commerce on familiar grounds of rate (*see, e.g., Associated Industries*, 511 U.S. 641), exemption (*see, e.g., Bacchus Imports*, 468 U.S. 263), or credit (*see, e.g., New Energy*, 486 U.S. 269), into a tax that discriminates on the ground of base. Consider, for example, *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984).

In *Armco*, the Court reviewed a West Virginia gross receipts tax imposed on various business activities in the State, including manufacturing and wholesaling. In-state manufacturers, however, were exempted from the tax on wholesaling. The Court struck down the exemption as unconstitutionally discriminatory. The Court reemphasized its long-standing doctrine that "a State may not tax a transaction

or incident more heavily when it crosses state lines than when it occurs entirely within the State." *Id.* at 642. The Court then noted that the challenged tax had "just this effect":

> The tax provides that two companies selling tangible property at wholesale in West Virginia will be treated differently depending on whether the taxpayer conducts manufacturing in the State or out of it. Thus, if the property was manufactured in the State, no tax on the sale is imposed. If the property was manufactured out of the State and imported for sale, a tax of 0.27% is imposed on the sale price.

Id. The Court went on to hold that the imposition of a higher in-state manufacturing tax did not eliminate the unconstitutional discrimination because the two taxes were not appropriate compensating taxes and when the two taxes were considered together, "discrimination against interstate commerce persist[ed]." *Id.* at 644.

But now assume that discrimination caused by a shifting tax base (such as Colorado's) that increases when economic activity occurs outside the State is constitutionally tolerable. West Virginia could now reenact its gross receipts tax, imposing it, as before, on both manufacturing and wholesaling, but without any exemption for manufacturers from the wholesaling tax, consistent with the Court's ruling. And, West Virginia could then achieve a comparable result as before if, like Colorado in the instant case, it imposed the tax only on the first taxable event in the State, whether that event is manufacturing or wholesaling. If a West Virginia manufacturer paid a West Virginia manufacturing tax on a "base" of $100 and sold the property in West Virginia for $200, it would owe no tax on the $200 wholesale sale, because it had already paid a tax to the State on the first taxable event (manufacturing). By contrast, an out-of-state manufacturer who sold property in West Virginia would pay a tax on a "base" of the $200 wholesale sale, because it would be the

first taxable event in the State. Although from an economic standpoint this is precisely the same tax discrimination that the Court struck down in *Armco*, it would survive scrutiny under the court of appeals' analysis because the discrimination is the function of a "shifting tax base"—a $100 base for the in-state manufacturer and a $200 base for the out-of-state manufacturer. As a matter of substance, of course, West Virginia would have simply exempted the in-state manufacturer from the wholesaling tax, which is precisely what *Armco* condemned as unconstitutional in another form. If the "practical or economic effect of the tax" (*Goldberg v. Sweet*, 488 U.S. 252, 262 (1989)), rather than "'magic words or labels'" (*Quill Corp. v. North Dakota*, 504 U.S. 298, 310 (1992) (quoting *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434, 441 (1959))), is to be the touchstone of Commerce Clause inquiry, the Colorado Court of Appeals' analysis cannot stand.

B. Permissible Discrimination Against Interstate Commerce By State Tax Schemes Would Have Real And Adverse Consequences For Our National Common Market

It is not just the ease with which the "shifting tax base" theory adopted by the court of appeals allows States to avoid the strictures of the dormant Commerce Clause that should be cause for concern. It is also, and in the end, more importantly, the consequences of this statutory legerdemain. This Court described those consequences in the very "shifting tax base" case to which we have already alluded, *Halliburton*. There the Court pointed out just what would happen if States could adopt taxes with bases (like the Colorado tax challenged here) that include the value of out-of-state but not equivalent in-state economic activity. *Halliburton*, 373 U.S. at 72-73.

First, even if only a single State were to impose "an additional tax burden for such out-of-state operations, the

disparate treatment would be an incentive to locate within" that State, and it would tend "'to neutralize advantages belonging to the place of origin.'" *Id.* at 72 (citation omitted). Of course, this Court's tax discrimination cases implicitly disapprove of such a result because a tax that is "'discriminatory in favor of the local merchant'" (*ibid.* (citation omitted)), encourages the out-of-state operator to move business into the State "in order to compete on equal terms." *Ibid.* In short, if the cost of out-of-state activities, but not equivalent in-state activities, is included in a State's "shifting tax base," there would be "an inexorable hydraulic pressure on interstate businesses to ply their trade within the State that enacted the measure rather than 'among the several States.'" *American Trucking Ass'ns v. Scheiner*, 483 U.S. 266, 286-287 (1987) (citation omitted).

Second, as this Court further observed in *Halliburton*, if other States adopted similar unequal tax structures—"a not unlikely result" if this Court were to affirm such a scheme—"the effects would be more widespread." *Halliburton*, 373 U.S. at 72. As *Halliburton* explained, "[t]he economic advantages of a single assembly plant" for multistate activities "would be decreased for units sent to every State other than the State of residence. At best, this would encourage the [taxpayer] to locate his assembly operations in the State of largest use for the units. At worst, it would encourage their actual fractionalization or discontinuance. Clearly, approval of [such a tax] would 'invite a multiplication of preferential trade areas destructive of the very purpose of the Commerce Clause.'" *Id.* at 72-73 (quoting *Dean Milk Co. v. Madison*, 340 U.S. 349, 356 (1951)).

CONCLUSION

For the reasons set forth above, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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April 7, 2006

APPENDIX

APPENDIX A

COLORADO COURT OF APPEALS
DIV. IV

No. 03CA2471

MCLANE WESTERN, INC.,
Plaintiff-Appellant,

v.

DEPARTMENT OF REVENUE OF THE STATE OF COLORADO; and M. MICHAEL COOKE, as the Executive Director of the Department of Revenue of the State of Colorado,
Defendants-Appellees.

May 5, 2005.
Certiorari Denied Jan. 9, 2006.

ROY, J.

Plaintiff, McLane Western, Inc., appeals the trial court's summary judgment in favor of defendants, the Department of Revenue of the State of Colorado and M. Michael Cooke, its Executive Director (collectively, the Department). We affirm.

The sole issue presented in this case is whether the excise tax imposed by Colorado on "the sale, use, consumption, handling, or distribution" of certain tobacco products in the state, § 39-28.5-102, C.R.S.2004, violates the Commerce Clause of the United States Constitution, U.S. Const. art. I, § 8, cl. 3. We conclude that it does not.

McLane buys, resells, and ships grocery products throughout the State of Colorado and other western states from its headquarters in Longmont, Colorado. As part of its opera-

tions, McLane buys tobacco products other than cigarettes, commonly referred to as "other tobacco products" (OTP), from manufacturers and suppliers and then resells them to its customers, primarily grocery and small convenience stores.

Prior to 1990, as relevant here, McLane purchased OTP directly from the United States Tobacco Company (U.S.T. Co.). U.S.T. Co. manufactured, marketed, and sold its products to unaffiliated distributors.

In 1990, U.S.T. Co. reorganized and formed two wholly-owned subsidiaries, United States Smokeless Tobacco Manufacturing, L.P. (Manufacturing) and United States Smokeless Tobacco Brands, Inc. (Sales). U.S.T. Co. also changed its name to United States Smokeless Tobacco Company (Smokeless Tobacco). After the reorganization, Manufacturing was responsible for manufacturing and packaging the products, and Sales was responsible for marketing and sales.

After Smokeless Tobacco reorganized and renamed itself, McLane purchased OTP from Sales. Sales purchased the OTP from Manufacturing at an invoice price that did not include any discounts or other reductions. Sales then resold the OTP at a higher price to McLane. According to Sales, this higher price reflected its own operating costs, profit margin, and the added value that came from its sales, marketing, distribution, and advertising efforts.

Manufacturing and Sales are located outside of Colorado, and the sale of OTP between them occurred outside of Colorado. McLane orders OTP from Sales, which ships the product to McLane in the state by common carrier. Upon the arrival at McLane's warehouse, McLane inspects and accepts or rejects the product.

McLane seeks refunds pursuant to § 39-28.5-101, *et seq.*, C.R.S.2004, of what it asserts were excess OTP excise taxes paid during various periods between 1990 and 2001. The OTP excise tax rate is twenty percent, which the Department

has assessed based on the manufacturer's or supplier's price paid by McLane to Sales.

McLane filed claims with the Department seeking a refund based upon its recalculation of the tax based on the price paid by Sales to Manufacturing, not on the higher price it paid to Sales. Using this recalculation, McLane claims a tax refund in the amount of $10,163,024.33 plus statutory interest. The Department denied the requests, and McLane commenced two actions, which have been consolidated. After agreeing to the material facts, the parties submitted cross-motions for summary judgment. The trial court granted the Department's motion. This appeal followed.

At the outset, we note that the parties have agreed that the price paid by Sales to Manufacturing meets the definition of "manufacturer's list price" as that term is defined by the applicable statute, § 39-28.5-101(3), C.R.S.2004. However, we recognize that in other contexts affiliated entities are considered a single economic entity. *See Copperweld Corp. v. Independence Tube Corp.*, 467 U.S. 752, 104 S.Ct. 2731, 81 L.Ed.2d 628 (1984)(affiliated entities cannot conspire for antitrust purposes because they are parts of a single entity); *Sec. Tire & Rubber Co. v. Gates Rubber Co.*, 598 F.2d 962 (5th Cir.1979) (Robinson-Patman Act price discrimination); *see also United States Tobacco Sales & Mktg. Co. v. State*, 96 Wash.App. 932, 982 P.2d 652 (1999) (price paid by Sales to Manufacturing may not reflect "fair market value" of promotional samples distributed by Sales for the purposes of OTP tax). We are, nonetheless, bound by the agreement of the parties.

Section 39-28.5-102, C.R.S.2004, provides:

> (1) There is levied and shall be collected a tax upon the sale, use, consumption, handling, or distribution of all tobacco products in this state at the rate of twenty percent of the manufacturer's list price of such tobacco

products. Such tax shall be imposed at the time the distributor:

> (a) Brings, or causes to be brought, into this state from without the state tobacco products for sale;
>
> (b) Makes, manufactures, or fabricates tobacco products in this state for sale in this state; or
>
> (c) Ships or transports tobacco products to retailers in this state to be sold by those retailers.

Section 39-28.5-101(2), C.R.S.2004, defines "distributor" as

> every person who first receives tobacco products in this state, every person who sells tobacco products in this state who is primarily liable for the tobacco products tax on such products, and every person who first sells or offers for sale in this state tobacco products imported into this state from any other state or country.

Section 39-28.5-101(3) defines "manufacturer's list price" as "the invoice price for which a manufacturer or supplier sells a tobacco product to a distributor exclusive of any discount or other reduction."

Summary judgment is appropriate only if the pleadings and supporting documents demonstrate that there is no genuine issue for trial as to any material fact and that the moving party is entitled to judgment as a matter of law. C.R.C.P. 56; *Bedard v. Martin*, 100 P.3d 584 (Colo.App.2004). Here, the parties agree that there is no dispute as to any material fact. We review orders granting summary judgment de novo. *Harding v. Heritage Health Prods. Co.*, 98 P.3d 945 (Colo. App. 2004).

I.

It has long been established that the Commerce Clause of the United States Constitution not only grants Congress the

authority to regulate commerce among the several states, but also limits the power of the states to discriminate against interstate commerce. *Riverton Produce Co. v. State*, 871 P.2d 1213 (Colo.1994). This latter limitation on the states is characterized as the "negative" aspect of the Commerce Clause and prohibits "economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors." *Riverton Produce Co. v. State, supra*, 871 P.2d at 1221 (quoting *New Energy Co. v. Limbach*, 486 U.S. 269, 273-74, 108 S.Ct. 1803, 1807, 100 L.Ed.2d 302 (1988)).

Thus, the United States Supreme Court has "characterized the fundamental command of the [Commerce] Clause as being that 'a State may not tax a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.'" *Assoc. Indus. v. Lohman*, 511 U.S. 641, 647, 114 S.Ct. 1815, 1820, 128 L.Ed.2d 639 (1994)(quoting *Armco Inc. v. Hardesty*, 467 U.S. 638, 642, 104 S.Ct. 2620, 2622, 81 L.Ed.2d 540 (1984)). This aspect of the Commerce Clause is frequently referred to as the "dormant Commerce Clause."

The dormant Commerce Clause does not, however, "immunize" all interstate commerce and its instrumentalities from state taxation. *Gen. Motors Corp. v. City & County of Denver*, 990 P.2d 59 (Colo.1999). "[A] state tax is not *per se* invalid because it burdens interstate commerce since interstate commerce may constitutionally be made to pay its way." *Maryland v. Louisiana*, 451 U.S. 725, 754, 101 S.Ct. 2114, 2133, 68 L.Ed.2d 576 (1981); *see also Riverton Produce Co. v. State, supra; Archer Daniels Midland Co. v. Colorado*, 690 P.2d 177 (1984).

A state's right to tax interstate commerce is limited, however, and no tax will be sustained unless it satisfies the four-part test announced by the Supreme Court in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 97 S.Ct. 1076, 51

L.Ed.2d 326 (1977). *Riverton Produce Co. v. State, supra.* Under *Complete Auto*, a state tax that impacts interstate commerce does not violate the dormant Commerce Clause if: (1) the tax is applied to an activity with a substantial nexus with the taxing state; (2) it is fairly apportioned; (3) it does not discriminate against interstate commerce; and (4) it is fairly related to the services provided by the taxing state. *Complete Auto Transit, Inc. v. Brady, supra; Riverton Produce Co. v. State, supra; Talbots, Inc. v. Schwartzberg*, 928 P.2d 822 (Colo.App.1996).

Here, McLane alleges that the OTP tax statute violates the third prong of the *Complete Auto* test, that is, it discriminates against interstate commerce. McLane argues that, because each layer in the distribution network marks up the price, the tax imposed on the product will be higher the later in that distribution network that one or more of the triggering events listed in § 39-28.5-102 occurs. Thus, the tax-liable distributor must pay the tax on the larger "tax base" created by the collective price mark-ups. There is no dispute that the tax rate remains constant.

For example, if the manufacturer and all the distributors were located within Colorado, the tax base would be at its lowest level. Thus, as McLane argues, and we agree, the location of the manufacturers, suppliers, or distributors involved in the product's distribution network and the price mark-up of each impacts the tax base or the price upon which the constant twenty percent tax rate is imposed. Consequently, McLane asserts, the OTP tax scheme discriminates against interstate commerce by creating an "inexorable pressure" on out-of-state businesses to move into the state to "take advantage of the overall OTP tax benefit." While we agree with McLane's assertions that the tax base will be higher the later in the distribution network the product is taxed, we disagree with McLane's conclusion that this fact renders the tax unconstitutional under the Commerce Clause.

A state tax violates the third prong of the *Complete Auto* test if it is facially discriminatory, has a discriminatory purpose, or has the effect of unduly burdening interstate commerce. *Riverton Produce Co. v. State, supra.* Although McLane argues in this instance that the OTP tax is discriminatory on its face, we conclude that it neither facially discriminates nor has the effect of discriminating against out-of-state competitors.

Our research, and our review of the authorities cited to us, leads us to conclude that a tax is discriminatory if it taxes out-of-state transactions or entities at a rate higher than it taxes in-state transactions, entities, or products, or if it exempts in-state transactions, entities, or products from an otherwise uniform tax. *See generally Fulton Corp. v. Faulkner*, 516 U.S. 325, 116 S.Ct. 848, 133 L.Ed.2d 796 (1996) (tax on a fraction of the value of corporate stock inversely related to the exposure of the corporation to state income tax is unconstitutional); *Assoc. Indus. v. Lohman, supra* (additional state use tax imposed on goods purchased out-of-state discriminates against interstate commerce in those counties in which local sales tax rates are less than the additional state use tax); *Ore. Waste Sys., Inc. v. Dep't of Envtl. Quality*, 511 U.S. 93, 114 S.Ct. 1345, 128 L.Ed.2d 13 (1994) (difference in rate of surcharge on in-state and out-of-state waste is unconstitutional); *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Fin.*, 505 U.S. 71, 112 S.Ct. 2365, 120 L.Ed.2d 59 (1992) (corporate income tax that taxed dividends from foreign subsidiaries but allowed deduction for dividends from domestic subsidiaries without a credit for taxes paid to foreign countries is unconstitutional under the Foreign Commerce Clause, U.S. Const. art. I, § 8); *Am. Trucking Ass'ns v. Scheiner*, 483 U.S. 266, 107 S.Ct. 2829, 97 L.Ed.2d 226 (1987) (flat axle tax discriminated against out-of-state truckers because the cost per mile exceeded that of in-state truckers); *Armco Inc. v. Hardesty, supra* (gross receipts tax imposed on businesses selling tangible property at wholesale

is unconstitutional because of exemption granted to in-state manufacturers); *Westinghouse Elec. Corp. v. Tully*, 466 U.S. 388, 104 S.Ct. 1856, 80 L.Ed.2d 388 (1984) (franchise tax credit lowering the effective tax rate for products shipped from a regular in-state place of business is unconstitutional); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 104 S.Ct. 3049, 82 L.Ed.2d 200 (1984) (tax on wholesale sales of liquor that exempted locally produced beverage is unconstitutional); *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318, 97 S.Ct. 599, 50 L.Ed.2d 514 (1977) (stock transfer tax that imposed different tax rates and ceilings depending on residence of seller or place of sale is unconstitutional); *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64, 83 S.Ct. 1201, 10 L.Ed.2d 202 (1963) (use tax on custom-made equipment manufactured out-of-state that included cost of labor and shop overhead in value taxed but excluded labor and shop overhead incurred in manufacturing such equipment in-state is unconstitutional); *see also* 1 Lawrence H. Tribe, *American Constitutional Law* § 6-15 (3d ed.2000) (discussing the implications of many of the cases cited).

In our view, while the tax here is imposed based on the price paid by the taxable distributor, neither Manufacturing or Sales is encouraged to move into the state because they might well become the taxable distributor. The tax is imposed on an activity within the state, the sale and distribution of OTP, not on the product or the distribution network. The fact that the tax base calculated on the price paid by the taxable distributor may place the product at a competitive disadvantage in the marketplace because the higher tax is added to the price does not, in our view, render the tax unconstitutional under the Commerce Clause. All taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion.

McLane's reliance on a line of United States Supreme Court cases finding violations of the Commerce Clause is not

persuasive. McLane cites *Armco Inc. v. Hardesty, supra*, where the state imposed a gross receipts tax on businesses selling tangible property at wholesale in the state, but exempted local manufacturers from paying the tax. Thus, the state gave local businesses a direct tax benefit that it did not give to out-of-state competitors. As the Court noted:

> On its face, the gross receipts tax at issue here appears to have just this [discriminatory] effect. The tax provides that two companies selling tangible property at wholesale in [the state] will be treated differently depending on whether the taxpayer conducts manufacturing in the State or out of it. Thus, if the property was manufactured in the State, no tax on the sale is imposed. If the property was manufactured out of the State and imported for sale, a tax of 0.27% is imposed on the sale price.

Armco Inc. v. Hardesty, supra, 467 U.S. at 642, 104 S.Ct. at 2622. Because an exemption to an otherwise uniform tax was granted to in-state companies in *Armco*, that case is not persuasive.

Likewise, in *Halliburton Oil Well Cementing Co. v. Reily, supra*, the taxpayer manufactured or assembled custom oil field equipment in another state. The State of Louisiana imposed a use tax on custom-made equipment manufactured out of, and brought for use into, the state. The value taxed on the out-of-state equipment was the total cost of manufacturing and assembling the equipment, including labor and shop overhead. However, with respect to such equipment manufactured in the state, the value did not include such costs. In addition, second-hand equipment was taxed differently based on whether it was purchased in or out of the state. The Court held the tax unconstitutional because it discriminated against out-of-state businesses and would encourage such businesses to move into the state. *See also Am. Trucking Ass'ns v. Scheiner, supra*, 483 U.S. at 286-87, 107 S.Ct. at 2842.

Here, however, the OTP tax scheme does not pressure out-of-state businesses to move to Colorado. Out-of-state manufacturers or distributors may engage in commerce within Colorado without suffering any burden from which local distributors or manufacturers are exempted.

The remaining cases upon which McLane relies are equally unavailing. None of them involves a determination that a state tax violates the Commerce Clause based on the inequities of a shifting tax base. Rather, they turn on unequal rates of taxation or exemptions from taxation for in-state businesses.

McLane also relies on *United States Tobacco Sales & Marketing Co. v. State, supra*, for the proposition that the price set by Manufacturing establishes the tax base. There, Sales distributed free samples of OTP at promotional events such as rodeos, auto races, and fishing tournaments. The question arose as to whether it should pay the OTP tax and, if so, on what base. Sales argued, as McLane argues here, that the correct tax base was the price it paid to Manufacturing. The trial court ruled that the correct basis was the price at which Sales sold the product to unaffiliated distributors.

The appellate court reversed, concluding that there were genuine issues of material fact as to the fair market value, rejected both parties' positions with respect to that issue, and remanded the matter for trial. We do not read the case as establishing Manufacturing's price as the appropriate tax basis under the circumstances presented here. There, Sales was the taxable distributor within the meaning of the Washington statute, and the tax base under that circumstance might well be the price it paid to Manufacturing.

Other states considering the constitutionality of similar OTP taxation statutes have upheld them under the Commerce Clause. In *Kansas Tobacco-Candy Distributors & Vendors,*

Inc. v. McDonald, 214 Kan. 67, 73, 519 P.2d 1110, 1115 (1974), the court stated:

> We do not see, however, how it can be said that the Tobacco Products Act of 1972 discriminates against firms engaged in an interstate business. The privilege tax applies equally to all distributors engaged in the business of selling or dealing in tobacco products in Kansas—to both resident and nonresident distributors. There is no differentiation between purchases made from Kansas manufacturers and purchases made outside Kansas in interstate commerce. All purchases without discrimination are taxed equally at an equal and constant tax rate of ten percent. The tax is imposed either at the time the tobacco distributor brings tobacco products into the state for sale or at the time a local distributor manufactures or fabricates tobacco products in this state for sale in this state. We find no basis for a charge of discrimination against interstate distributors. Furthermore we find nothing in the record to show that distributors of tobacco products in interstate commerce are in any way unduly burdened by the statutory privilege tax imposed.

Similarly, in *McLane Co. v. Washington State Department of Revenue*, 105 Wash.App. 409, 19 P.3d 1119 (2001), the appellate court found that a similar tax did not violate the Commerce Clause. There, McLane argued that the tax was unconstitutional because it was incurred by merely placing an order. The court disagreed, stating:

> But the tax is not levied on the purchase order. Although the tax is "imposed at the time" a distributor "brings or causes to be brought" tobacco products into Washington for sale under RCW 82.26.020(2), the taxable event is the "sale, use, consumption, handling, or distribution of . . . tobacco products." RCW 82.26.020(1). . . . As the Washington Supreme Court has

> explained, "any wholesaler or any retailer who brings or causes tobacco products to be brought into the state from an out-of-the-state source becomes liable for the tax when such tobacco products are brought into the state." *Galvin v. Tax Comm'n*, 56 Wash.2d 738, 740, 355 P.2d 362 (1960). Thus, the purchase order is not the taxable event and the tax is not upon commerce itself. We hold that the OTP tax is not an unconstitutional tax against interstate commerce.

McLane Co. v. Wash. State Dep't of Revenue, supra, 105 Wash.App. at 414-15, 19 P.3d at 1121.

We also note that unsuccessful challenges to a similar OTP tax have been made in Illinois on state constitutional grounds. *Arangold Corp. v. Zehnder*, 204 Ill.2d 142, 272 Ill.Dec. 600, 787 N.E.2d 786 (2003)(due process and uniformity claims; unspecified federal claims abandoned); *Arangold Corp. v. Zehnder*, 187 Ill.2d 341, 240 Ill.Dec. 710, 718 N.E.2d 191 (1999) (single subject provision of state constitution).

Therefore, we conclude that the tax imposed on OTP pursuant to § 39-28.5-101, et seq., does not violate the Commerce Clause of the United States Constitution.

II.

McLane also argues that the plain language of the term "manufacturer's list price" mandates that the invoice price Sales paid to Manufacturing be the price at which the tax base is set. In so arguing, McLane asserts that the trial court "need not reach the term 'supplier' because the facts established an earlier qualifying sale between a manufacturer and a distributor." Thus, McLane argues, "[t]here simply is no reason to move to the second transaction when the first transaction fixes the tax base."

We disagree with McLane's construction of the statute and agree with the trial court that the presence of the term

"supplier" in the statutory definition of "manufacturer's list price" necessarily imposes the tax on the price McLane paid to Sales. We cannot ignore the plain language of § 39-28.5-101(3). When construing a statute, we must presume the General Assembly meant what it clearly said and did not use language idly. *In re Marriage of Mugge*, 66 P.3d 207 (Colo.App.2003). Here, McLane purchased the OTP from a supplier, not a manufacturer, of the product. Accordingly, the price that McLane paid Sales is the "manufacturer's list price" for purposes of the statute.

Having so concluded, we need not address McLane's remaining arguments.

The judgment is affirmed.

Judge WEBB and Judge GRAHAM concur.

APPENDIX B

DISTRICT COURT
CITY AND COUNTY OF DENVER, COLORADO

[Filed November 7, 2003]

Case Number: 02 CV 5118
(consolidated with 02 CV 5777)
Courtroom 18

MCLANE WESTERN, INC.,

Plaintiff,

v.

DEPARTMENT OF REVENUE OF THE STATE OF COLORADO and M. MICHAEL COOKE as the Executive Director of the Department of Revenue of the State of Colorado,

Defendants.

ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

The State of Colorado imposes a 20% excise tax on tobacco products other than cigarettes ("other tobacco products" or "OTP"). C.R.S. § 39-28.5-101 et seq. Plaintiff McLane Western, Inc. is a distributor of other tobacco products and paid the tax for most of the 1990's. McLane brings this suit for refund of its alleged over-payment of tobacco excise taxes, claiming it used an incorrect tax base. The Colorado Department of Revenue denies that any refund is due.

These consolidated cases were set for trial. Prior to trial, the parties agreed that there are no genuine disputes as to the material facts and that the matter could be determined on cross-motions for summary judgment. Therefore the trial was vacated, and a hearing on the cross-motions for summary judgment was held on October 23, 2003.

UNDISPUTED MATERIAL FACTS

I agree that the material facts are not in dispute and that the issue may be decided a matter of law. The material undisputed facts are as follows:

1. McLane buys, resells and ships grocery products including smokeless tobacco products, or OTP, throughout the western United States, including Colorado. McLane currently employs 583 persons in Colorado and owns or operates numerous offices, warehouses and equipment throughout Colorado. McLane's principal place of business in Colorado is located in Longmont.

2. McLane is a distributor of OTP in Colorado under Colorado's OTP statute.

3. U.S. Smokeless Tobacco Company is a wholly-owned subsidiary of UST, Inc., a publicly traded corporation. Prior to 1990, U.S. Smokeless Tobacco Company (then known as United States Tobacco Company) performed all functions relating the manufacture, marketing and sale of its smokeless tobacco products, primarily branded as Skoal and Copenhagen. Until 1990, U.S. Smokeless Tobacco Company marketed and sold the OTP that it had manufactured directly to distributors like McLane. Effective January 1, 1990, U.S. Smokeless Tobacco Company reorganized and formed two wholly-owned subsidiaries, U.S.T. Manufacturing and U.S.T. Sales. Following the reorganization, U.S.T. Manufacturing assumed the tobacco manufacturing functions while U.S.T. Sales separately assumed the tobacco marketing and sales functions. In February 1990, U.S. Smokeless Tobacco Company notified state taxing authorities that the UST companies had reorganized, that U.S.T. Sales was responsible for selling the OTP, that U.S.T. Manufacturing was responsible for manufacturing the OTP and that each subsidiary operated as a separate legal entity. The UST companies announced the reorganization to the general public in their annual report and SEC filings at the same time.

4. For all of the refund periods in dispute, McLane purchased the subject OTP exclusively from U.S.T. Sales. McLane then resold the OTP to its customers. Most of McLane's customers in Colorado are small convenience stores and grocery stores.

5. U.S.T. Manufacturing has been the sole manufacturer of the subject OTP. U.S.T. Manufacturing sells the OTP it manufactures exclusively to U.S.T. Sales for resale and distribution in the United States. U.S.T. Manufacturing does not manufacture any tobacco products in Colorado.

6. Since the 1990 reorganization, U.S.T. Sales has engaged in the business of marketing and selling OTP primarily to other distributors, such as McLane, which then resell the product to retailers. U.S.T. Sales purchases the OTP that it markets and resells exclusively from U.S.T. Manufacturing. U.S.T. Sales has its principal place of business in Greenwich, Connecticut and has approximately thirty employees regularly working throughout Colorado.

7. For all of the refund periods in dispute, U.S.T. Manufacturing manufactured and sold the OTP at issue to U.S.T. Sales exclusively. The prices charged by U.S.T. Manufacturing to U.S.T. Sales from the sale of the OTP did not include any discount or other reduction. U.S.T. Manufacturing invoiced U.S.T. Sales on a monthly basis, and U.S.T. Sales paid these invoices on a quarterly or monthly basis. U.S.T. Manufacturing provides its prices to its customers, including U.S.T. Sales, to McLane and similar second-tier distributors with a legitimate business need for the information, and to state taxing authorities upon request.

8. For all of the refund periods in dispute, U.S.T. Sales charged McLane its distributor's list price, which was higher than U.S.T. Manufacturing's price for a number of reasons, including the cost and added value of the marketing, sales and distribution functions performed by U.S.T. Sales.

9. By way of illustration, on December 26, 1996, U.S.T. Manufacturing charged U.S.T. Sales a price of $145.33 for a 180-can case of "premium" OTP. On that same date, U.S.T. Sales charged McLane $352.80 for the same 180-can case. The details of the OTP products, prices and refunds claimed for the relevant periods are reflected in Exhibit A attached to the Koch affidavit submitted with McLane's motion for summary judgment.

10. For the refund periods in dispute, the total amount charged by U.S.T. Sales to McLane was $95,160,668.50. McLane paid total OTP tax of $19,032,122.70. Had the OTP tax been calculated on the price paid by U.S.T. Sales to U.S.T. Manufacturing, the total OTP tax would have been $8,518,660.25.

11. After accounting for the 3.5% vendor deduction, McLane claims it is due a total refund of $10,163,024.33 plus statutory interest.

12. The general steps of each sale transaction between U.S.T. Sales and McLane were as follows:

- When it received a purchase order from McLane, U.S.T. Sales ordered the OTP requested from U.S.T. Manufacturing. Acting as agent for U.S.T. Sales, U.S.T. Manufacturing then arranged, at U.S.T. Sales' expense, for the OTP to be shipped by common carrier to McLane's warehouse in Colorado.

- On delivery of the OTP to the common carrier at the dock of one of U.S.T. Manufacturing's facilities located outside of Colorado, U.S.T. Manufacturing transferred ownership (including title and risk of loss) of the OTP to U.S.T. Sales. U.S.T. Sales retained ownership (including title and risk of loss) of the OTP during shipment to McLane's warehouse in Longmont, Colorado. U.S.T. Sales also bore the cost of shipping the OTP to McLane.

- When the OTP shipment arrived at McLane's warehouse in Colorado, McLane's employees inspected the shipment. If the OTP was in good condition and the quantity verified, McLane accepted delivery of the shipment.

- Upon McLane's acceptance of delivery at its dock in Colorado, U.S.T. Sales transferred ownership (including title and risk of loss) of the OTP to McLane in Colorado. McLane typically paid U.S.T. Sales within seven days of the date of invoice.

13. From March 1990 through September 1993 and March 1996 through December 1997, McLane calculated and paid the OTP excise tax based on the price it paid to U.S.T. Sales. On April 2 and 13, 1999, McLane submitted claims to the Department seeking a refund based on recalculating the tax on the price paid by U.S.T. Sales to U.S.T. Manufacturing. On October 14, 1999, the Department denied McLane's claims for refund. These refund claims are the subject of Civil Action No. 02-CV-5118.

14. On April 19 and June 14, 2002, McLane submitted supplemental refund claims for the periods January 1998 through March 1999 and April 1999 through December 2001. The Department denied McLane's supplemental claims on June 18 and July 23, 2002. These refund claims are the subject of Civil Action No. 02-CV-5777.

15. On November 22, 2002, this Court consolidated the two actions.

THE STATUTORY SCHEME

The excise tax on other tobacco products is levied by C.R.S. §39-28.5-102 which provides as follows:

Tax levied. (1) There is levied and shall be collected a tax upon the sale, use, consumption, handling, or distribution of all tobacco products in this state at the rate of twenty percent

of the manufacturer's list price of such tobacco products. Such tax shall be imposed at the time the distributor:

> (a) Brings, or causes to be brought, into this state from without the state tobacco products for sale;
>
> (b) Makes, manufactures, or fabricates tobacco products in this state for sale in this state; or
>
> (c) Ships or transports tobacco products to retailers in this state to be sold by those retailers.

"Distributor" is defined by the statute as "every person who first receives tobacco products in this state, every person who sells tobacco products in this state who is primarily liable for the tobacco products tax on such products, and every person who first sells or offers for sale in this state tobacco products imported into this state from any other state or country." C.R.S. §39-28.5-101(2).

"Manufacturer's list price" is defined as "the invoice price for which a manufacturer or supplier sells a tobacco product to a distributor exclusive of any discount or other reduction." C.R.S. §39-28.5-101(3).

McLane argues that U.S.T. Sales is a "distributor" under the statute because it first sells tobacco products imported into this state from any other state or country. It is undisputed that the sale from U.S.T. Sales to McLane takes place in Colorado since title does not transfer to McLane from U.S.T. Sales until the product reaches McLane's warehouse in Longmont. Since U.S.T. Sales is a distributor, McLane argues that it should have computed the tax based on the manufacturer's list price paid by U.S.T. Sales to U.S.T. Manufacturing.

The Department initially argued that the statute contemplates there being only one distributor for any given transaction and that McLane, not U.S.T. Sales, was the distributor for the subject transactions. At the hearing, I rejected that reading of the definition of distributor. The Department now

argues that, even if U.S.T. Sales is a distributor, McLane is the distributor liable for the tax and that the appropriate tax base is McLane's price to its supplier, U.S.T. Sales. McLane responds that this interpretation of the statute as applied to these transactions would violate the commerce clause by imposing a burden on interstate commerce.

RULES OF STATUTORY CONSTRUCTION

The rules of statutory construction applicable here are familiar. When a court construes a statute, it must give effect to the intent of the General Assembly. *A.B. Hirschfeld Press v. Denver*, 806 P.2d 917, 920 (Colo. 1991). The words of a statute are to be given "their commonly accepted and understood meaning." *Adams v. Farmers Ins. Group*, 983 P.2d 797, 801 (Colo. 1999). C.R.S. §2-4-101 provides that a statute's "words and phrases shall be read in context and construed according to the rules of grammar and common usage." When interpreting a comprehensive legislative scheme, a court must give meaning to all of the statute's parts and construe them together as a whole. *See, e.g., Huddleston v. Grand County Bd. of Equalization*, 913 P.2d 15, 18 (Colo. 1996).

In the event of a constitutional challenge, a statute is presumed to be constitutional. *Board of County Commissioners v. Vail Associates, Inc.*, 19 P.3d 1263, 1272-1273 (Colo. 2001). The party challenging the constitutionality of a statute has the burden of proving it unconstitutional beyond a reasonable doubt. *Alexander v. Industrial Claims Appeals Office*, 42 P.3d 46, 48 (Colo. App. 2001). If possible, a court must construe a statute in the manner that does not invalidate it. *BQP Indus., Inc. v. State Board of Equalization*, 694 P.2d 337, 343 (Colo. App. 1984).

CONCLUSIONS OF LAW

Having reviewed the briefs and attachments and considered the arguments of counsel and the relevant authorities, and keeping in mind the foregoing rules of statutory construction,

I make the following conclusions of law on the issues presented by the cross-motions for summary judgment.

First, I agree with McLane that U.S.T. Sales fits the definition of "distributor" under the statute. U.S.T. Sales makes the first sale in Colorado of tobacco products imported into this state. The Department's argument that that portion of the definition of distributor should be construed as applying only to products imported into this state to be resold to retailers by the distributor is simply adding additional language to the statute that the legislature did not use. However, I also conclude that U.S.T. Sales, for the purposes of these transactions, is a "supplier" as that term is used in the definition of "manufacturer's list price." The statute does not include any definition of the term "supplier," but supplier is not a technical or obscure term and should be given its common sense meaning. "Supplier" is a noun form of the verb "supply" which means to furnish or provide something. *Webster's College Dictionary* (Random House, 1996). U.S.T. Sales clearly furnishes or provides the OTP to McLane. McLane's argument essentially tries to ignore the presence of "supplier" in the definition of "manufacturer's list price."

The Department argues that since McLane owes the tax, the tax base should be the price McLane pays to its supplier. There seems to be no doubt that McLane owes the tax, and it does not argue to the contrary. The tax is imposed upon the sale, handling or distribution of other tobacco products in Colorado, and McLane performs all three of those incidences of taxation. It is irrelevant, in my view, that U.S.T. Sales might also owe the tax as a seller or distributor of OTP. This case is about what McLane owes, and specifically, the tax base to be used for McLane's payment of the tax.

The three subparagraphs of C.R.S. §39-28.5-102 are called incidences of taxation by the Department and timing of tax payment by McLane. Whatever they are, McLane fits two of those and U.S.T. Sales fits none. McLane fits the category

described in subparagraph (a) because it "brings, or causes to be brought, into this state from without the state tobacco products for sale." The Washington courts have construed this same language in a case involving McLane, although the Washington statute uses the language as one of the statutory definitions of "distributor." In *McLane Company, Inc. v. Washington State Department of Revenue*, 19 P.3d 1119, 1121 (Wash. App. 2001), the Washington Court of Appeals held that McLane was a distributor because it brought or caused to be brought into Washington the tobacco products for resale in Washington. The court rejected McLane's argument that the supplier who owns the products when they arrive in Washington (UST Sales) fits that definition of distributor.

Obviously, McLane also ships or transports tobacco products to retailers in Colorado to be sold by those retailers (subparagraph (b) of §39-28.5-102) while U.S.T. Sales does not. Neither McLane nor U.S.T. Sales makes, manufactures or fabricates tobacco products in Colorado for sale in Colorado (subparagraph (c) of §39-28.5-102). Therefore, the statute contemplates that it is McLane's activities, not the activities of U.S.T. Sales, that trigger payment of the tax.

Given this interpretation of the statute, what tax base does the statute require McLane to use to compute the tax? McLane argues that it should use, not the price it pays, but the price U.S.T. Sales pays to U.S.T. Manufacturing. This argument seems to be premised on reading the definition of "manufacturer's list price" as being restricted to the first sale by *a* manufacturer (UST Manufacturing) to *a* distributor (UST Sales) without regard to who is liable for payment of the tax. Adopting McLane's position would require a strained and unnatural interpretation of the statute. For McLane as a distributor, its "manufacturer's list price" is the price for which its supplier (U.S.T. Sales) sells product to McLane. If the term "supplier" were not in the definition of manufacturer's

list price, McLane's argument that it should use its distributor's purchase price as McLane's tax base would carry weight. However, I cannot ignore the legislature's inclusion of the term "supplier" or its natural application here.

It is a sensible construction of the statute that the price paid by the distributor who owes the tax should be the tax base. This interpretation finds support in C.R.S. §39-28.5-106 which requires that the quarterly returns of the tax must show "the total amount of tobacco products purchased by the distributor during the preceding quarter and the tax due thereon." The return need not reflect the total amount of tobacco products purchased by the distributor's supplier or any other third party. Further, it is unreasonable to expect that a distributor would be required to pay a tax based on a transaction to which it was not a party. Although in this case, U.S.T. Manufacturing apparently makes its list price available to distributors like McLane as well as state taxing authorities, it is certainly possible that a manufacturer of other tobacco products would not readily disclose its price to an unrelated mid-level distributor occupying the position of U.S.T. Sales. McLane has not cited any other excise tax scheme which operates in the unusual manner which McLane proposes here.

For these reasons, I find and conclude that the appropriate tax base is the one used by McLane for ten years, that is, McLane's price paid to U.S.T. Sales. Therefore, McLane is not due any refund.

COMMERCE CLAUSE

McLane argues strenuously that the Department's interpretation of the statute is unconstitutional because it violates the commerce clause. There is no doubt that state taxes which discriminate against interstate commerce by taxing a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the state are constitutionally invalid under the commerce clause. *Associated Indus. of Mo.*

v. Lohman, 511 U.S. 641, 647 (1994). While some earlier interpretations urged by the Department may have suffered from this infirmity, the interpretation I adopt does not. My interpretation of the statute does not depend on where the manufacturer (U.S.T. Manufacturing) or the supplier (U.S.T. Sales) resides or does business or where the sale to McLane takes place. Both U.S.T. Sales and U.S.T. Manufacturing could be located in Colorado or they could both have no contact whatsoever with Colorado. The tax base for McLane would be the same: the price it pays to its supplier. These facts and this interpretation simply do not implicate the commerce clause. McLane posits a variety of hypotheticals that might create problems under the commerce clause. I decline to speculate on how the statute should operate on factual scenarios which are not before me.

Likewise, the foregoing interpretation of the statute does not violate anyone's right to equal protection under the laws; similarly situated distributors will be treated identically.

For all the foregoing reasons, McLane's motion for summary judgment is denied and the Department's cross-motion for summary judgment is granted. McLane's complaints are dismissed with prejudice. Costs are awarded to the Department.

SO ORDERED.

Dated this 7th day of November, 2003.

BY THE COURT:

/s/ Joseph E. Meyer III
JOSEPH E. MEYER III
District Court Judge

cc: Thomas H. Steele, Counsel for Plaintiff
Andrew W. Swain, Counsel for Defendant

APPENDIX C

DISTRICT COURT
CITY AND COUNTY OF DENVER, COLORADO

Case Number: 02 CV 5118
(consolidated with 02 CV 5777)
Courtroom 18

MCLANE WESTERN, INC.,
Plaintiff,

v.

DEPARTMENT OF REVENUE OF THE STATE OF COLORADO and M. MICHAEL COOKE as the Executive Director of the Department of Revenue of the State of Colorado,
Defendants.

ORDER

This matter is before the Court on plaintiff's motion to alter or amend judgment. Defendants have moved to strike that motion as not being consistent with Rule 59, C.R.C.P. The motion to strike is denied. The motion to alter or amend judgment is also denied.

SO ORDERED.

Dated this 9th day of Jan., 2004.

BY THE COURT:

/s/ Joseph E. Meyer III
JOSEPH E. MEYER III
District Court Judge

cc: Thomas H. Steele, Counsel for Plaintiff
Andrew W. Swain, Counsel for Defendant

APPENDIX D

SUPREME COURT, STATE OF COLORADO

[Filed January 9, 2006]

No. 05SC439

MCLANE WESTERN, INC.,

Petitioner,

v.

DEPARTMENT OF REVENUE OF THE STATE OF COLORADO; and M. MICHAEL COOKE, as the Director of the Department of Revenue of the State of Colorado,

Respondents.

ORDER OF COURT

Upon consideration of the Petition for Writ of Certiorari to the Colorado Court of Appeals and after review of the record, briefs, and the judgment of said Court of Appeals,

IT IS THIS DAY ORDERED that said Petition for Writ of Certiorari shall be, and the same hereby is, DENIED.

BY THE COURT, EN BANC, JANUARY 9, 2006.

Copies mailed via the State's Mail Services Division on 01/09/06. MLK

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Clerk of the Court
Colorado Court of Appeals

APPENDIX E

Relevant portions of the Colorado statutes, Sections 101 and 102 of Title 39, Article 28.5, Tax on Tobacco Products of 1986, in effect for all tax periods at issue, provide:

COLORADO REVISED STATUTES
TITLE 39—TAXATION
SPECIFIC TAXES
TOBACCO TAX
ARTICLE 28.5—TAX ON TOBACCO PRODUCTS

39-28.5-101. Definitions

As used in this article, unless the context otherwise requires:

(1) "Department" means the department of revenue.

(2) "Distributor" means every person who first receives tobacco products in this state, every person who sells tobacco products in this state who is primarily liable for the tobacco products tax on such products, and every person who first sells or offers for sale in this state tobacco products imported into this state from any other state or country.

(3) "Manufacturer's list price" means the invoice price for which a manufacturer or supplier sells a tobacco product to a distributor exclusive of any discount or other reduction.

(4) "Sale" means any transfer, exchange, or barter, in any manner or by any means whatsoever, for a consideration, including all sales made by any person. The term includes a gift by a person engaged in the business of selling tobacco products, for advertising, as a means of evading the provisions of this article or for any other purposes whatsoever.

(5) "Tobacco products" means cigars, cheroots, stogies, periques, granulated, plug cut, crimp cut, ready rubbed, and other smoking tobacco, snuff, snuff flour, cavendish, plug and twist tobacco, fine-cut and other chewing tobaccos, shorts,

refuse scraps, clippings, cuttings and sweepings of tobacco, and other kinds and forms of tobacco, prepared in such manner as to be suitable for chewing or for smoking in a pipe or otherwise, or both for chewing and smoking, but does not include cigarettes which are taxed separately pursuant to article 28 of this title.

39-28.5-102. Tax levied

(1) There is levied and shall be collected a tax upon the sale, use, consumption, handling, or distribution of all tobacco products in this state at the rate of twenty percent of the manufacturer's list price of such tobacco products. Such tax shall be imposed at the time the distributor:

(a) Brings, or causes to be brought, into this state from without the state tobacco products for sale;

(b) Makes, manufactures, or fabricates tobacco products in this state for sale in this state; or

(c) Ships or transports tobacco products to retailers in this state to be sold by those retailers.

3

Supreme Court, U.S.
FILED
JUN 7 - 2006
OFFICE OF THE CLERK

NO. 05-1294

IN THE SUPREME COURT OF THE UNITED STATES

MCLANE WESTERN, INC.,
Petitioner

vs.

COLORADO DEPARTMENT OF REVENUE, STATE OF COLORADO; AND M. MICHAEL COOKE AND FRED FISHER, AS THE EXECUTIVE DIRECTORS OF THE DEPARTMENT OF REVENUE OF THE STATE OF COLORADO

Respondents.

On Petition for Writ of Certiorari to
The Colorado Court of Appeals

BRIEF OF THE RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Colorado imposes a tax on the price paid by the first Colorado distributor for certain tobacco products. Depending on the distributor's business practices, this price may be paid to a manufacturer or a supplier. The price paid to a supplier will generally be higher, reflecting markups added throughout the product distribution chain. The question presented is whether the state's imposition of this tax on a supplier's price violates the United States Constitution's grant to Congress of the power "[t]o regulate Commerce . . . among the several States." U.S. Const. art. I, § 8, cl. 3.

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STATEMENT

1. Counterstatement of the Facts

Petitioner McLane's statement of the factual background omits important information regarding the relationship between the supplier and the manufacturer from which McLane bought "other tobacco products" ("OTP") during the periods at issue. Before 1990, McLane purchased OTP from the United States Tobacco Company ("USTCo."). Pet.'s Appendix A at 2a. At that time, USTCo. sold OTP to unaffiliated distributors such as McLane. *Id.* USTCo. performed three functions: manufacturing OTP, marketing it, and selling it. *Id.* In January 1990, USTCo. reorganized and formed two wholly-owned subsidiary companies, United States Tobacco Sales & Marketing Company, Inc. ("UST Sales") and United States Tobacco Manufacturing Company, Inc. ("UST Manufacturing"). *Id.*

The subsidiaries' parent company, USTCo., changed its name to U.S. Smokeless Tobacco Company ("US Smokeless"). *Id.* UST Sales assumed USTCo.'s marketing and sales functions while UST Manufacturing assumed USTCo.'s manufacturing function. *Id.* UST Sales purchased OTP exclusively from its affiliate, UST Manufacturing. Pet.'s Appendix B at 16a, ¶¶ 5, 7. UST Sales then sold the OTP to distributors such as McLane. *Id.* at 16a, ¶ 5. After USTCo.'s reorganization, McLane continued to purchase OTP from USTCo., but through its affiliate, UST Sales. Pet.'s Appendix A at 2a. For all the refund periods in dispute, McLane purchased OTP exclusively from UST Sales. *Id.*

UST Sales sold OTP to McLane at a higher price than UST Manufacturing sold the same OTP to its affiliate, UST Sales. *Id.* at 2a. McLane explains the higher price as

reflecting the costs specific to UST Sales' marketing and selling functions. *Id.*; *see also* Pet.'s Appendix B at 16a, ¶ 8. The implication is that, in the pre-1990 OTP transactions, when USTCo. (now U.S. Smokeless) sold OTP to McLane, the price: (1) included the costs associated with manufacturing as well as those associated with marketing and selling since, at the time, USTCo. performed all three functions, and (2) was not significantly different from the price for which McLane purchased the OTP from UST Sales. McLane never challenged these assumptions throughout the state court proceedings.

McLane buys, resells, and ships grocery products, OTP among them, throughout the Western United States, including Colorado. Pet.'s Appendix A at 1a. McLane initially calculated its OTP tax liability using, as the law requires, the price it actually paid for the OTP, which was the invoice price of the supplier, UST Sales. At some point, however, McLane had the revelation that it could lower its tax liability by basing its calculation not on the price it actually paid, but on the lower manufacturer's invoice price that UST Manufacturing charged its own affiliate, UST Sales. Pet.'s Appendix B at 17a, ¶¶ 9-10; 18a, ¶ 13. The difference in these invoice prices is the basis for McLane's refund claims. *Id.*

2. Counterstatement of Colorado's OTP-Tax Scheme.

McLane fails to adequately explain the manner in which Colorado imposes its OTP tax on the price a distributor pays in order to purchase OTP. Colorado imposes a tax on the "manufacturer's list price" for OTP when a distributor first performs any one of three incidences of taxation related to the distribution of OTP that are listed in Colo. Rev. Stat. § 39-28.5-102(1)(a)-(c): bringing OTP into the state for sale, manufacturing OTP in the state, or

transporting OTP to retailers in the state. McLane concedes that it performs at least two of these activities and is therefore liable for the tax associated with its OTP purchases from UST Sales. Pet.'s Appendix A at 3a.

Colorado law defines "manufacturer's list price" as "the invoice price for which a manufacturer *or supplier* sells a tobacco product to a distributor exclusive of any discount or other reduction." Colo. Rev. Stat. § 39-28.5-101(3) (emphasis added). *See also* Pet.'s Appendix A at 4a. The statute includes this dual specification to ensure that companies cannot avoid their obligation to pay the tax simply by reorganizing into separate manufacturing and supply subsidiaries, as USTCo. did. The statutory structure therefore seeks to achieve the same result no matter what the structure of the manufacturing and supply system from which a distributor purchases OTP—that is, the law seeks to impose the tax on the price actually paid for OTP by the taxable distributor. Many other states impose an OTP tax in a similar manner.[1]

Under this system, determining the tax base requires only ascertaining what price the distributor responsible for the OTP tax paid for OTP. In this case, McLane, the party admittedly responsible for paying the OTP tax, purchased OTP from UST Sales. Pet.'s Appendix B at 18a, ¶ 13. McLane paid UST Sales for OTP, and UST Sales provided McLane an invoice for OTP. *Id.* at 17a-18a, ¶¶ 12, 13. Accordingly, pursuant to Colorado's definition of

---

[1] *See, e.g.*, Cal. Rev. & T. Code § 30011.7 (OTP tax imposed on the cost of tobacco products the taxable distributor pays for OTP); Md. Tax–General Code Ann. § 12-101(g) (tax imposed on the price the taxable wholesaler pays for OTP); Neb. Rev. Stat. § 77-4008 (the tax is imposed on the purchase price paid by the OTP's first owner); N.M. Stat. Ann. §§ 7-12A-2, 7-12A-3 (the tax is imposed on the "product value," which means the amount paid for the OTP); N.C. Gen. Stat. § 105-113.4(2) (tax imposed on the price paid for OTP by the taxable person); Or. Rev. Stat. Ann. § 323.500(15) (tax imposed on price paid for untaxed tobacco products), and W. Va. Code §§ 11-17-2, 11-17-3 (if the taxpayer purchases OTP from any one other than a manufacturer, the tax is imposed on the invoice price paid by the taxpayer).

"manufacturer's list price," the invoice price paid by McLane determined its OTP tax. McLane has never purchased OTP from UST Manufacturing; therefore, whatever price UST Manufacturing might charge *its sister subsidiary is not* relevant to calculating McLane's tax liability.

REASONS FOR DENYING THE WRIT

The decision of the Colorado Court of Appeals is correct and does not conflict with any decision of this Court or the courts of any other state. Further review is therefore not warranted. The central premise of McLane's claim is that an earlier sale and purchase of OTP between UST Sales and UST Manufacturing, a sale not involving the undisputed taxpayer, McLane, somehow should determine the tax base upon which McLane calculates its OTP-tax liability. Basing a taxpayer's burden on an ancillary transaction that does not involve the taxpayer would be novel in the area of transactional and excise taxes. Nothing in the Commerce Clause or this Court's precedent requires or justifies such a strange result.

I. The Colorado Decision Does Not Discriminate Against Interstate Commerce And, Therefore, Does Not Raise A Constitutional Question.

A. Colorado's OTP-Tax Scheme Focuses On The Actions Of In-state Distributors And Those Distributors' Performance Of In-state Incidences Of Taxation Rather Than On The Actions Performed By Out-Of-State Suppliers.

The Petition asserts that "[t]he disparate treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter is undisputed in this case." Pet. at 9. This is simply untrue. It is undisputed that in some hypothetical cases the OTP-tax system would tax in-state OTP manufacturers at a lower base than it would tax in-state distributors. But the Respondents have consistently argued that the general effect of the OTP tax is not to favor in-state economic interests. Indeed, as will be shown below, it is at least as likely that the high levels of taxation of in-state activity related to the manufacture, sale, and distribution at issue here serves to discourage such activity in Colorado.

The record contains no evidence that any OTP manufacturers exist in Colorado. Though the case does not turn on this fact, it is unlikely that the state created this scheme to benefit nonexistent entities. The facts, as clarified above, show that Colorado's OTP-tax scheme is structured so tobacco manufacturers, suppliers, and distributors cannot avoid their liability simply by effecting artificial corporate reorganizations. Despite McLane's efforts to paint Colorado's OTP-tax scheme as a jumble of "shifting tax

bases," the scheme is, in fact, a straightforward transaction tax. Like any other such tax, it applies only to the activities of those doing business within the jurisdiction of the taxing entity.

To determine liability under the OTP-tax scheme, two questions must be answered. First, who is liable for the tax? The answer is the distributor who first brings OTP into Colorado, manufactures OTP in Colorado, or transports OTP to retailers in Colorado. *See* Colo. Rev. Stat. § 39-28.5-102(1)(a)-(c). Once the entity liable for the tax is determined, the second question is simple: What did that entity pay for the OTP? *See id.* §§ 39-28.5-101(3); -102(1).

It is obvious from these questions that the location of an entity is relevant only in answering the first question: Who pays? This answer must take into account whether an activity is taking place inside or outside Colorado, not for discriminatory purposes but for simple jurisdictional ones. Colorado does not seek to tax out-of-state activities. Apparently conceding this, McLane's entire petition focuses on the second question: How much? But in answering this question, the location of the entities is irrelevant. All that matters is the price McLane paid for the OTP. The fact that USTCo.'s reorganization resulted in one out-of-state affiliated company charging another a lower price than McLane pays does not change the fact that Colorado must tax the actual invoice price paid by McLane, the in-state distributor.

The OTP tax does not violate the test established by this Court in *Complete Auto Works v. Brady* 430 U.S. 976, 97 S. Ct. 1669 (1977). In that case, this Court ruled that a state can impose its transaction taxes on activities that cross state borders as long as the activities do not discriminate against interstate commerce. *Id.* at 279. The Colorado Court of Appeals' construction of Colorado's OTP-tax scheme ensures that the tax base is determined by the OTP purchase

price paid by the in-state entity that performs one of the three incidences of taxation (who then owes the tax) and therefore has nexus with Colorado sufficient to the state's compelling compliance with its OTP-tax scheme in a constitutionally permissible manner. The OTP-tax scheme's focus on in-state incidences of taxation places the responsibility for paying the OTP tax on in-state distributors rather than those of out-of-state suppliers. It does this in order to tax in-state incidences of taxation rather than to tax OTP as it enters Colorado as part of interstate commerce or tax the distribution network itself. Pet.'s Appendix A at 8a.

Contrary to McLane's assertions, the proper application of the Court of Appeals' construction of the OTP-tax scheme does not depend on whether the supplier or manufacturer resides inside or outside Colorado, or whether the sale of OTP to a Colorado distributor was consummated inside or outside the state. The proper application depends on identifying: (a) the single in-state distributor that pays the OTP tax on a particular transaction, and (b) what price that tax-liable distributor pays for the OTP. The Court of Appeals correctly concluded this when it held that "[a]ll taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion." *Id.*

B. Colorado's OTP-Tax Scheme Does Not Favor In-state Economic Interests Over Out-Of-State Interests.

McLane mistakenly asserts that the Court of Appeals' interpretation of Colorado's OTP-tax scheme discriminates against interstate commerce by favoring in-state economic interests over out-of-state interests. Pet. at 14. The Court of Appeals correctly concluded that "neither [UST] Manufacturing nor [UST] Sales is encouraged to move into [Colorado] because they might well become the

taxable distributor." Pet.'s Appendix A at 8a. The court is correct.

If anything, the OTP scheme would discourage OTP manufacturers and suppliers from moving to Colorado. Were an OTP manufacturer or supplier to do so, pursuant to the mandates in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), its presence in Colorado would subject it to the state's taxing authority. To particularize the hypothetical, if UST Manufacturing (or UST Sales) moved to Colorado, it would become the taxable distributor under Colo. Rev. Stat. §§ 39-28.5-101(2) and -102. Perhaps this explains the apparent paradox in McLane's argument, which hinges on Colorado's discriminating in favor of an in-state industry that does not exist.

McLane premises its assertions on the Court of Appeals' acknowledgement that, since the OTP tax is calculated using the OTP's purchase price, OTP purchased and taxed at the end of a long distribution supply chain will have a higher price and a resultant higher tax than OTP purchased and taxed at the end of a short distribution and supply chain. Pet. at 7, 14. It is true that, as the OTP passes through a supply chain, the OTP's ultimate taxable price accumulates middlemen's markups. Accordingly, as the Court of Appeals concluded, a product that has a higher sales tax because of a long distribution and supply chain will likely be at a competitive disadvantage to one that has a lower sales tax due to a shorter distribution and supply chain. Pet.'s Appendix A at 8a. But the Court of Appeals correctly held that, because the competitive disadvantage is a product of McLane's decision to purchase OTP through a distribution supply chain rather than directly from a manufacturer, this disadvantage does not violate the Dormant Commerce Clause. In other words, the court correctly concluded that the higher tax McLane wishes to

avoid is of its own making and a product of its own OTP purchasing model, not Colorado's OTP-tax scheme.

A similar competitive disadvantage arises in the context of another excise tax—that is, the sales and use tax. Taxing jurisdictions impose their sales tax on the price at which retailers sell their product to the ultimate consumer.[2] The retail purchase price, like OTP's purchase price, reflects an accumulation of markups imposed by middlemen suppliers (called wholesalers) as the product passes through the distribution and supply chain. The fewer the middlemen, the lower the price the retailer charges its customers and the lower the sales tax associated with the sales price. There is nothing unconstitutional about imposing transactional taxes, including the OTP tax, on a marked-up price.

Correctly viewing Colorado's OTP-tax scheme reveals that it and the decision upholding it are not blueprints by which states can construct discriminatory and, therefore, unconstitutional transactional-tax systems. The scheme is a rational way for states to combat companies' continuing attempts to avoid or limit their state tax liabilities through creative and sometimes questionable tax planning.

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[2] *See, e.g.*, Colorado's sales- and use-tax scheme which defines "purchase price" as the price charged the consumer and as the amount of money received or due in order to purchase a product or taxable service. Colo. Rev. Stat. § 39-26-102(7)(a) and 1 Colo. Code Regs. 201-4 § 26-102.7(a)(1). *See also* the *Streamlined Sales and Use Tax Agreement*, Appendix C, p. 83 (Nov. 12, 2002) (available at <http://www.streamlinedsalestax.org/Final%20Agreement%20As%20Amended%2001-13-06.pdf>), which defines "sales price" as the amount of money for which goods and property are sold and includes the price the seller paid for the property and the seller's service costs. In both these examples, the taxable price would include the seller's mark-up.

II. There Is No Conflict With This Court's Decisions.

A. The Ruling Below Does Not Conflict With Halliburton Oil Well Cementing Co. v. Reily.

McLane mistakenly asserts that the Court of Appeals' decision "is contrary to" the holding in 373 U.S. 64 (1963). Pet. at 10. In *Halliburton Oil Well Cementing Company v. Reily*, 373 U.S. 64, 83 S.Ct. 1201 (1963), the taxpayer manufactured or assembled custom oil field equipment outside Louisiana. The state imposed a use tax on custom-made equipment manufactured outside Louisiana and brought into the state for use. The tax on the out-of-state equipment was based on the total cost of manufacturing and assembling the equipment, including labor and shop overhead. However, the taxable price of equipment manufactured in Louisiana did not include these added costs. In addition, second-hand equipment was taxed differently based on whether it was purchased in or out of the state. This Court held the tax unconstitutional because it discriminated against out-of-state businesses and encouraged businesses to move into the state.

Colorado's OTP-tax scheme, however, does not pressure out-of-state businesses to move to Colorado. In fact, as discussed above, the opposite may well be true. It may be helpful to consider how, exactly, the facts in *Halliburton* would have to be adjusted for it to be the twin of the case at hand. Louisiana would have to have had a consistent tax rate based on the price paid for goods brought from outside the state for sale in Louisiana. The plaintiff would have to have claimed that its tax liability should be based not on the price it paid for the goods, but on some lower price paid by another entity outside the state. The other entity would have to be an affiliate of the company from which the plaintiff

actually bought the goods, and the three would have had exclusive sales contracts with one another. Needless to say, this Court would not have analyzed this hypothetical case in a way remotely similar to the way it analyzed the real facts in *Halliburton*.

Another hypothetical scenario demonstrates the type of shifting tax base that McLane complains would violate the holding in *Halliburton*. Assume for example that Colorado's OTP-tax scheme provided that in-state distributors must use the manufacturer's invoice price in order to calculate their OTP taxes, but that out-of-state distributors with Colorado nexus must use the supplier's invoice price to calculate their taxes. Also assume that this statutorily mandated use of different tax bases resulted in in-state distributors paying a tax lower than the out-of-state distributors. This would be a shifting tax base, and it would violate the holding in *Halliburton* and the Dormant Commerce Clause because it would give in-state distributors a tax advantage over out-of-state distributors with Colorado nexus. In other words, in this hypothetical, Colorado's OTP-tax scheme would mandate a competitive advantage for in-state distributors.

In actuality, however, Colorado's tax scheme does not mandate a disparity in the treatment of distributors similar to that addressed in *Halliburton*. The Court of Appeals correctly determined that "[a]ll taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion." Pet.'s Appendix A at 8a. The shifting tax base about which McLane complains is a result of its decision to purchase OTP via an artificial supply chain, not a product of Colorado's OTP-tax scheme. The Colorado Court of Appeals correctly ruled that *Halliburton* does not conflict with its decision. Pet.'s Appendix A at 9a-10a.

B. The Ruling Below Does Not Conflict With *Armco Inc. v. Hardesty*.

McLane mistakenly asserts that the Court of Appeal's decision violates the holding in *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984). Pet. at 16-18. In *Armco, Inc.*, this Court struck down West Virginia's gross receipts tax as discriminating against interstate commerce because the state exempted in-state manufacturers from gross receipts tax when they sold their locally manufactured products in West Virginia, but required out-of-state manufacturers who had nexus with West Virginia to pay the tax when they sold in the state products manufactured outside the state. *Id.* at 639, 640. Colorado's OTP-tax scheme does not discriminate because, unlike the tax scheme at issue in *Armco*, it does not distinguish between local, in-state distributors and out-of-state distributors. All similarly situated tax-liable distributors are treated the same.

This type of tax-imposition scheme satisfies the mandates of the Dormant Commerce Clause. All in-state distributors and the out-of-state distributors with Colorado nexus are liable for the OTP tax. Colorado does not exempt one party while requiring the other to pay the tax. The only differential treatment is between those who are taxed (distributors engaging in taxable activity in Colorado) and those who are not (those not engaging in taxable activities in the state). Whatever the Dormant Commerce Clause is meant to do, it is not to prevent states from taxing in-state activities. The Colorado Court of Appeals correctly applied *Armco*. Pet.'s Appendix A at 7a-8a.

III. The Question Presented To This Court Has Not Been Properly Developed In The Lower State Court Proceedings And Involves A Unique OTP Distribution Structure.

McLane asks this Court to invalidate Colorado's OTP-tax scheme and issue a decision that prevents states such as Colorado from imposing their OTP taxes on the price in-state taxable distributors pay for OTP. McLane wants this Court to do this based on an insufficient record and a unique factual situation. But because the record before the Court has not been properly developed and involves a unique OTP purchasing structure, the decision below does not merit this Court's attention.

The record from the proceedings below contains no evidence explaining why McLane does not purchase OTP directly from a manufacturer as it did prior to USTCo.'s 1990 reorganization. There is no evidence that a manufacturer would sell OTP directly to McLane for the lower price at which it seeks to be taxed. That is, there is no evidence that there exists a real market for OTP at a price any different from that at which McLane now purchases OTP from a supplier. Indeed, fundamental economics suggests that the price McLane pays is the market price for the OTP it is purchasing. But the price McLane seeks to use as its tax base is the price set by an artificial supply chain comprised of related corporate entities that buy and sell only from one another. There is no evidence that other OTP manufacturers sell their product to taxable distributors via an artificial supply chain comprised of related entities as does USTCo. Neither is there evidence that other taxable distributors purchase OTP via a supply chain comprised of either related or unrelated entities rather than directly from a manufacturer.

The record provides no evidence indicating whether the claim asserted by McLane represents anything more than a unique situation, one caused entirely by: (1) USTCo.'s corporate structure, a structure that creates an artificial supply chain intended to give USTCo. and its customers various tax advantages, and (2) McLane's inexplicable devotion to purchasing OTP at a "higher price" caused by the product's travels through this artificial supply chain.[3] The Colorado Court of Appeals correctly applied state law to prevent McLane from taking advantage of the artificial manufacture, supply, and distribution structure created by USTCo. in order to avoid fully paying the state's OTP tax. This Court should not accede to McLane's desires and issue a wide-ranging opinion based on the limited record below and the unique factual situation it presents.

IV. There Is No Conflict Among The States On The Question Presented By McLane.

McLane implicitly recognizes that there is no precedent supporting its premise that a state cannot impose an OTP tax or any other transactional tax on the actual price paid by a taxpayer for a taxable item. *See* Pet. at 14. No contradictory precedent exists because no state or other court has invalidated a similar transactional-tax scheme on such grounds. Accordingly, this Court should decline to review this case because the Colorado Court of Appeals has not decided an important question of federal law in conflict with the decision of any other state court. *See* U.S. Sup. Ct. R. 10 (b).

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[3] Furthermore, during the litigation before the Denver District Court, the Respondents conceded, for purposes of the summary judgment, that UST Sales purchased OTP from its affiliate UST Manufacturing in an arm's-length transaction. The Colorado Court of Appeals correctly noted in its opinion this concession's uniqueness when it said that a similar transaction between related entities could be conducted at less than arm's length. Pet.'s Appendix A at 3a. This unusual concession further demonstrates the limited record on which McLane asks this Court to issue a wide-ranging opinion, and makes it unlikely that any decision this Court renders would resolve the issue for future litigants.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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IN THE

Supreme Court of the United States

MCLANE WESTERN, INC.,
Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF COLORADO, *ET AL.*,
Respondents.

On Petition for a Writ of Certiorari to the Colorado Court of Appeals, Division IV

REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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RULE 29.6 CORPORATE DISCLOSURE STATEMENT

McLane Western, Inc. has set forth its Rule 29.6 corporate disclosure statement in its Petition for a Writ of Certiorari, filed April 7, 2006.

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REPLY BRIEF OF PETITIONER

Petitioner McLane Western, Inc. respectfully replies to the opposition of respondents the Colorado Department of Revenue and M. Michael Cooke, in her official capacity as Executive Director of the Colorado Department of Revenue, to petitioner's request for a Petition for a Writ of Certiorari to review the judgment of the Colorado Court of Appeals as follows:

Respondents' attempts to defend the erroneous constitutional ruling of the court below are contrary to this Court's bedrock Commerce Clause jurisprudence, and do not distinguish *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), or *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984), both of which condemn taxing schemes functionally identical to Colorado's. Respondents do not dispute the central feature of the Colorado taxing regime that lies at the heart of this case, namely, that the State's tax base (and therefore the tax) is increased when more of the distribution chain is located outside of Colorado and decreased when more of the distribution chain is located within the State. Indeed, respondents could hardly contend otherwise, because to do so would fly in the face of the court of appeals' determination that "if the manufacturer and all the distributors were located within Colorado, the tax base would be at its lowest." Pet. App. at 6a. It is this undisputed (and indisputable) fact of an inverse relationship between tax liability and in-state economic activity that runs counter to Commerce Clause doctrine and warrants this Court's review. *See* Brief of the American Trucking Associations, Inc., *et al.*, as *Amici Curiae* in Support of Petitioner at 4-6 (analyzing flawed constitutional analysis and significant adverse impact of the court of appeals' ruling).

I. COLORADO'S DISCRIMINATORY TAX CANNOT BE DEFENDED ON THE THEORY THAT PETITIONER MIGHT HAVE AVOIDED IT

While conceding that petitioner has suffered a competitive disadvantage as a result of Colorado's discriminatory tax regime, respondents nevertheless seek to defend the tax discrimination on the ground that "the competitive disadvantage is a product of McLane's decision to purchase * * * through a distribution supply chain rather than directly from a manufacturer." Br. in Opp. at 8. According to respondents, petitioner's claim fails under the Commerce Clause because "the higher tax McLane wishes to avoid is of its own making and a product of its own * * * purchasing model" and "not Colorado's * * * tax scheme." *Id.* at 8-9.

Respondents' argument fails on two counts. First, the infirmity in Colorado's taxing scheme is not that it favors one "purchasing model" over another, but that it favors supply chains with more *in-state* links over identical supply chains with more *out-of-state* links. The court of appeals explicitly recognized this fact in observing that "the tax base will be higher the later in the distribution network the product is taxed" (Pet. App. at 6a), and that "if the manufacturer and all of the distributors were *located in Colorado*, the tax base would be at its lowest." *Ibid.* (emphasis added).[1]

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[1] Respondents' suggestion that, notwithstanding the offer of a lower tax base, Colorado's taxing regime might actually discourage manufacturers and suppliers from moving to Colorado, because they would become subject to a tax they could otherwise avoid (Br. in Opp. at 8, 10), misses the economic point. Of course they would be subject to tax, but to a lower tax than otherwise would be due from McLane if these out-of-state entities had remained outside the State. And that lower tax could be passed on to McLane who would economically benefit, as McLane no longer would be liable for the greater tax because it no longer would be the distributor first engaging in taxable activity in the State. *See* Brief of Washington Legal Foundation as *Amicus Curiae* in Support of Petitioner at 11-12 (describing

Second, the suggestion that petitioner might have avoided the discriminatory impact of Colorado's tax by restructuring its operations to purchase products at an earlier point in the distribution chain is no defense to Commerce Clause discrimination. Forcing taxpayers to choose between subjecting themselves to a discriminatory tax or rearranging their affairs to avoid the exaction plainly "forecloses tax-neutral decisions," *Boston Stock Exchange v. State Tax Commission*, 429 U.S. 318, 331 (1977), thereby undermining our national common market. This Court has specifically held that a victim's ability to circumvent discrimination by yielding to its illicit incentives cannot save an impermissibly discriminatory tax. *See Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Fin.*, 505 U.S. 71, 78 (1992) (there is "no authority" for proposition that a discriminatory tax "may be upheld if the taxpayer could avoid that discrimination by changing the [corporate] domicile").

II. THE SUPERFICIAL NEUTRALITY OF COLORADO'S TAX DOES NOT SHIELD IT FROM CONDEMNATION AS A LEVY THAT DISCRIMINATES AGAINST INTERSTATE COMMERCE

In their Opposition, respondents make much of the fact that the Colorado taxing scheme has a superficial neutrality, because it applies to the distributor who first engages in taxable activity in Colorado at whatever price the distributor paid for the product. "[D]etermining the tax base requires only ascertaining what price the distributor responsible for the * * * tax paid for OTP" (Br. in Opp. at 3); "[a]ll that matters is the price McLane paid for the OTP" (*id.* at 6); and "'[a]ll taxable distributors * * * are taxed at the same rate and on a tax base determined in the same fashion.'" *Id.* at 7

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the economic consequences of an out-of-state distributor submitting to Colorado's excise tax).

(quoting Pet. App. at 8a). But respondents (like the court below) ignore the critical underpinnings of this Court's contemporary Commerce Clause jurisprudence in suggesting that the superficial neutrality of a tax can protect it from Commerce Clause attack, when the practical effect of the levy is to discriminate against interstate commerce.

In its modern Commerce Clause opinions, this Court has repeatedly emphasized that "the Commerce Clause has a deeper meaning that may be implicated even though state provisions * * * do not allocate tax burdens between insiders and outsiders in a manner that is facially discriminatory." *American Trucking Ass'ns, Inc. v. Scheiner*, 483 U.S. 266, 281 (1987). Accordingly, the Court has embraced a decisional framework that has increasingly "considered not the formal language of the tax statute but rather its practical effect." *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). Indeed, the Court has explicitly rejected respondents' "focus on * * * formalism [that] merely obscures the question whether the tax produces a forbidden effect." *Id.* at 288.

In *American Trucking Associations*, for example, the Court struck down "facially neutral," 483 U.S. at 269, flat taxes on interstate motor carriers. Like Colorado's levy at issue here, the flat taxes were superficially neutral, because the same tax applied to all trucks, whether intrastate or interstate. But the Court found that the challenged taxes necessarily disadvantaged interstate truckers, who traveled fewer miles in the State than did their intrastate competitors, because the interstate truckers paid a substantially higher effective per-mile tax. Thus the Court observed:

> Although out-of-state carriers obtain a privilege to use Pennsylvania's highways that is nominally equivalent to that which local carriers receive, imposition of the flat taxes for a privilege that is several times more valuable to a local business than to its out-of-state competitors is

> unquestionably discriminatory and thus offends the Commerce Clause.

Id. at 296.

Similarly, in *Nippert v. City of Richmond*, 327 U.S. 416, 430-35 (1946), the Court struck down a facially neutral municipal tax imposed on those engaging in business as solicitors on the ground that the tax in its "practical operation worked discriminatorily against interstate commerce." *Id.* at 425. The Court observed: "To ignore the variations in effect which follow from application of the tax, uniform on the face of the ordinance, * * * is only to ignore these practical consequences." *Id.* at 431.

In this case, respondents do not (and cannot) dispute the fact that Colorado's tax increases when more links in the distribution chain are located outside the State and decreases when more links in the distribution chain are located within the State. A clearer example of discrimination in effect would be difficult to imagine, and "[a]ctual discrimination, wherever it is found, is impermissible," *Associated Industries of Missouri v. Lohman*, 511 U.S. 641, 650 (1994), even when the statutes causing such discrimination are superficially neutral.

III. COLORADO'S EXCISE TAX DISCRIMINATION BROADLY AFFECTS COLORADO DISTRIBUTORS AND CANNOT BE DEFENDED AS A LEGITIMATE ANTIDOTE TO TAX MANIPULATION

Respondents argue that Colorado's discrimination is unworthy of review because there is "no evidence indicating" that petitioner's grievance is not a "unique situation," stemming from "an artificial supply chain" (Br. in Opp. at 13, 14) created by petitioner's supplier to produce an excise tax advantage. *Id.* at 14. On a related note, respondents urge the

Court to overlook the disparate tax burdens borne by in-state and out-of-state distribution because Colorado's "shifting tax base" is "a rational way for States to combat * * * continuing attempts to avoid or limit their state tax liabilities through creative and sometimes questionable tax planning." *Id.* at 9.

Wholly apart from the impropriety of making unfounded factual allegations without record support at this late stage of the proceedings, not to mention the questionable relevance of the alleged tax planning of petitioner's *supplier* to the discrimination visited upon *petitioner* by Colorado's taxing regime, available information shows that these allegations have no basis in fact. First, a Washington Court of Appeals opinion addressing this very same "supply chain" in the context of Washington's excise tax reveals that petitioner's supplier first learned of the excise tax consequences of the reorganization of its manufacturing and distribution operations from a state tax auditor *six years after the reorganization had occurred. United States Tobacco Sales & Mktg., Inc. v. Department of Revenue*, 982 P.2d 652, 654-55 (Wash. Ct. App. 1999). Plainly, it was something other than excise tax planning that motivated the reorganization of petitioner's supplier.

Second, in the proceedings below, respondents stipulated that the transactions between petitioner's supplier and the manufacturer were conducted at "arm's length." Br. in Opp. at 14 n.3. This concession contradicts respondents' belated characterization of the transactions at issue as "artificial."

Third, the *amicus* filing in this case by the Colorado Association of Distributors, among others, demonstrates that the discrimination suffered by petitioner does not arise from a "unique situation" involving an "artificial supply chain." The brief shows that the Colorado scheme in fact discriminates against a broad array of other Colorado distributors who acquire similar products from out-of-state distributors and are forced to pay "a higher tax than they would pay were the

tobacco products manufactured or first distributed in Colorado." *See* Brief of the Colorado Association of Distributors as *Amicus Curiae* in Support of Petitioner at 1-2.

Fourth, respondents' own Brief in Opposition refers to numerous other state excise tax statutes that employ a similar "shifting tax base." Br. in Opp. at 3 n.1. These statutes, like Colorado's, are not confined to allegedly "artificial" transactions employed to produce excise tax advantages, and their existence reinforces the significance of this case and the need for this Court's review. *See* Brief of Washington Legal Foundation as *Amicus Curiae* in Support of Petitioner at 4.

Finally, even if Colorado had a legitimate concern with excise tax manipulation, it is not free to adopt discriminatory tax measures to address that concern. The Court's cases "leave open the possibility that a State may validate a statute that discriminates against interstate commerce by showing that it advances a legitimate local purpose that cannot be adequately served by *reasonable nondiscriminatory alternatives*." *New Energy Co. v. Limbach*, 486 U.S. 269, 278 (1988) (emphasis added). There are a number of reasonable nondiscriminatory alternatives available to the State to impose an excise tax on other tobacco products while still protecting the tax from "questionable tax planning" (Br. in Opp. at 9), such as a per-unit tax, a value-based tax imposed at a single point in a distribution chain that does not vary with its location within or without the State, or a retail sales tax. *See* Pet. at 13.[2]

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[2] Respondents err in contending that the competitive disadvantage of which petitioner complains "arises in the context of * * * the sales and use tax" (Br. in Opp. at 9), because the typical sales and use tax differs in a dispositive respect from Colorado's excise tax. The sales tax is always imposed upon the final sales price to the consumer, and thus even-handedly captures each middleman's markup, regardless of whether those middlemen are located within or without the State. Contrary to respondents' assertions, petitioner is not objecting to the taxation of the

IV. RESPONDENTS' EFFORTS TO DISTINGUISH *HALLIBURTON* AND *ARMCO* ELEVATE FORM OVER SUBSTANCE

Respondents' efforts to distinguish *Halliburton* and *Armco* elevate form over substance and ignore the teachings of this Court's Commerce Clause jurisprudence.

A. The Facts Of *Halliburton* Are In Substance Identical To The Facts Of This Case

To avoid the controlling force of *Halliburton*, respondents offer two hypothetical scenarios upon which they rely to distinguish the facts of this case from those of *Halliburton*. Br. in Opp. at 10-11. Respondents then claim that these differences somehow demonstrate that Colorado's statute passes muster. *Ibid.* Wholly apart from the point that the argument rests on a *non sequitur*—because some other hypothetical tax scheme violates the Commerce Clause, this one does not—the hypotheticals offered by respondents are in substance no different from the facts of this case and reaffirm the discriminatory nature of the Colorado scheme.

Respondents claim that "the facts in *Halliburton* would have to be adjusted" in a number of ways "for it to be the twin of the case at hand." *Id.* at 10. But the only facts to which respondents point either are *identical* to the facts of this case or have nothing to do with the substance of the operation of the statutes in the two cases. Thus respondents contend that "Louisiana would have to have had a consistent tax rate based on the price paid for goods brought from outside the state for sale in Louisiana." *Ibid.* In fact, Louisiana *did* have a consistent tax rate—two percent—for such goods. *See* Pet. at 11. Respondents further claim that to make

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"marked-up price." *Ibid.* Petitioner is objecting to a tax imposed on the markup only when the "middleman" is located out of State. And it is that mechanism which violates the Commerce Clause.

this case the "twin" of *Halliburton*, the taxpayer in *Halliburton* would have had to claim tax liability based on the price paid under exclusive contracts by some other entity who was affiliated with the entity from which the taxpayer bought the goods. Br. in Opp. at 10-11. But these are matters of form that have nothing to do with the constitutional infirmity in this case or in *Halliburton*, to wit, that the tax base increased in *Halliburton* because assembly activity occurred outside Louisiana, just as the tax base increased in the instant case because the distribution activity occurred outside Colorado. Similarly, the second hypothetical offered by respondents, where they *concede* that discrimination exists (*id.* at 11), focuses largely on matters of form that would simply make the discrimination that exists in this case more transparent.

In the end, respondents' attempt to deflect the Court's attention from the clear application of *Halliburton* to this case turns entirely on their unjustifiably narrow focus on the superficially neutral form of the Colorado statute. Respondents never advance their argument beyond repetition of the mantra of the court below that "'[a]ll taxable distributors * * * are taxed at the same rate and on a tax base determined in the same fashion.'" Br. in Opp. at 7, 11 (quoting Pet. App. at 8a). For the reasons set forth above, such a preoccupation with the form of the tax while ignoring its substance has no place in the Court's contemporary Commerce Clause jurisprudence and would undermine the Court's holding in *Halliburton*.

B. The Facts Of *Armco* Are In Substance Identical To The Facts Of This Case

Respondents' perfunctory effort to distinguish *Armco* is also unsuccessful. Br. in Opp. at 12. Respondents focus entirely on the *form* of the discrimination at issue while ignoring its *substance*. Thus respondents contend that the discrimination at issue in *Armco* is distinguishable from the

discrimination at issue in the instant case because there is no formal exemption in the Colorado statute (as there was in the statute in *Armco*) for those engaged in in-state activity.

But for the reasons set forth above and in the Petition (*see* Pet. at 17-18), this is a distinction without a constitutional difference. It is the "practical or economic effect of the tax[,]" *Goldberg v. Sweet*, 488 U.S. 252, 262 (1989), not "formal distinctions that lack economic substance[,]" *Westinghouse Electric Co. v. Tully*, 466 U.S. 388, 405 (1984), which is the touchstone of Commerce Clause analysis. The favoritism for in-state manufacturers/wholesalers under West Virginia's taxing scheme in *Armco* is economically indistinguishable from the favoritism for in-state manufacturers/distributors under Colorado's taxing scheme here. Both violate settled Commerce Clause doctrine articulated by this Court.

CONCLUSION

For the foregoing reasons and the reasons raised in the Petition for a Writ of Certiorari, the Petition for a Writ of Certiorari should be granted.

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(2)

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In the Supreme Court of the United States

MCLANE WESTERN, INC.,

Petitioner,

v.

DEPARTMENT OF REVENUE; STATE OF COLORADO, *ET AL.*

Respondents.

On Petition for a Writ of Certiorari to the Colorado District Court of Appeals, Division IV

BRIEF OF THE AMERICAN TRUCKING ASSOCIATIONS, INC., AND THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA AS *AMICI CURIAE* IN SUPPORT OF PETITIONER

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QUESTION PRESENTED

Whether a facially neutral state tax that is structured in such a way that it invariably imposes a greater burden on interstate businesses than on identical businesses that confine their operations to the taxing state violates the Commerce Clause of the U.S. Constitution.

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INTEREST OF THE *AMICI CURIAE*[1]

American Trucking Associations, Inc. (ATA) is a non-profit corporation incorporated under the laws of the District of Columbia, with its principal place of business in Alexandria, Virginia. ATA is the national trade association of the trucking industry. It has more than 2,000 direct motor carrier members and, in cooperation with state trucking associations and affiliated national trucking conferences, ATA represents tens of thousands of motor carriers. ATA was created to promote and protect the interests of the trucking industry, which consists of every type and geographical scope of motor carrier operation in the United States, including for-hire carriers, private carriers, leasing companies and others. ATA regularly advocates the trucking industry's position before this and other courts.

Interstate commercial operations of the trucking industry are massive in size and scope. As of July 2004, the U.S. Department of Transportation's Federal Motor Carrier Safety Administration had on file 524,309 registered interstate motor carriers. Almost eight billion tons of freight, with a value of $6.2 trillion, moved by truck in interstate commerce in 2002. U.S. Department of Transportation & U.S. Department of Commerce, *2002 Commodity Flow Survey*, at Table 1a. Millions of shipments per day are necessary to move that volume of freight and service the needs of the American economy.

ATA and its members have a critical interest in the protection of interstate commercial activity against all forms of

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[1] Pursuant to Rule 37.6 of the Rules of this Court, *amici* state that this brief was not authored in whole or in part by counsel for a party and that no person or entity, other than the *amici curiae*, their members, and their counsel made a monetary contribution to its preparation and submission. The written consents of the parties to the filing of this brief have been filed with the Clerk of the Court.

discriminatory state taxation and regulation. Discrimination that impedes the free flow of products in interstate commerce negatively affects the trucking industry in the same manner as does direct discrimination against interstate trucking itself. The interstate trucking industry historically has been one of the principal targets of discriminatory state taxation and regulation. As a result, ATA and its members have brought or participated in Commerce Clause challenges to a wide range of state taxes, fees, and regulations before this Court and other state and federal courts.

The Chamber of Commerce of the United States of America is the world's largest business federation, representing a membership of more than three million businesses and organizations of every size, in every industry sector and geographical region of the country. A central function of the Chamber is to represent the interests of its members in important matters before the courts, Congress, and the Executive Branch. To that end, the Chamber has filed *amicus* briefs in numerous cases in this Court addressing issues of vital concern to the Nation's business community, and has regularly participated in cases involving the meaning of the Commerce Clause.

The Chamber has a substantial interest in the issue presented in this case: businesses in all sectors of the economy have been affected by state taxes that discriminate against interstate commerce in their practical effects. Such discrimination, moreover, discourages the conduct of business across state lines and works a substantial drag on the national economy. The Chamber believes that the experience of its members with these problems makes it well situated to address the issues presented here.

STATEMENT

This case involves a challenge to a Colorado tax on activities related to the distribution of certain tobacco products in the State. Insofar as is relevant here, the tax is collected

from the person in the distribution chain who "first receives" the products in Colorado. Colo. Rev. Stat. §29-28.5-101, 102. During the time at issue in this case, the tax was imposed at a rate of twenty per cent on the price paid by the first Colorado distributor of the products.

Under this tax regime, the more that is done to the product (for example, marketing, sales, and distribution activity) outside Colorado, the higher the price of the product will be when it finally reaches and is "first receive[d]" by a distributor in the State – and the higher the tax due on the product will be. The court below recognized this, acknowledging that, "if the manufacturer and all the distributors were located within Colorado, the tax base would be at its lowest level." Pet. App. 6a. That is so because the tax is imposed only once per product, and when manufacturing and all distribution of the product takes place in Colorado, the tax is calculated at the time of first in-state distribution on the basis of a price that has not yet been inflated by the mark-ups related to transportation, marketing, and related activities that inevitably take place along the distribution chain. Thus, as petitioner explains (at Pet. 4), this tax structure means that the tax base is higher (and the amount collected correspondingly greater) when more of the products' distribution chain is located outside Colorado.

Petitioner brought this suit in Colorado state court, contending that the Colorado tax is unconstitutional under the Commerce Clause of the U.S. Constitution because it discriminates against interstate commerce in its practical effect. The trial court upheld the tax (Pet. App. 14a-25a) and the Colorado Court of Appeals affirmed. *Id.* at 1a-13a. The court of appeals recognized that, under the Colorado scheme, "the location of the manufacturers, suppliers, or distributors involved in the product's distribution network" has an impact on the size of the tax base and that, as a consequence, "the tax base will be higher the later in the distribution network the product is taxed." *Id.* at 6a. The court also acknowledged

that this regime "may place the product" that is distributed interstate "at a competitive disadvantage in the marketplace because the higher tax is added to the price." *Id.* at 8a. But the court nevertheless held the Colorado tax constitutional because it does not "tax[] out-of-state transactions or entities at a rate higher than it taxes in-state transactions, entities, or products, or * * * exemp[t] in-state transactions, entities, or products from an otherwise uniform tax." *Id.* at 7a.

REASONS FOR GRANTING THE PETITION

The Colorado tax imposes an obvious impediment to interstate commerce; the court below itself candidly acknowledged that the levy places products at a competitive disadvantage if more of their distribution chain is located out of state. This discriminatory impact on goods that are moved interstate should render the Colorado tax unconstitutional. In reaching the contrary conclusion, the court below was of the view that a tax's discrimination against interstate commerce in practical effect is immaterial so long as the levy does not *overtly* accord interstate commerce disparate treatment. But that conclusion, which invites states to develop subtle means of discrimination against interstate businesses, surely is wrong. Because the decision below illustrates a resistance to fundamental Commerce Clause principles that is found in many state tax regimes – and because it adopts an approach to the Clause that is inconsistent with the imperative for a uniform national economy that the Constitution was designed to foster – further review is warranted.

A. The Colorado Tax Imposes Discriminatory Burdens On Interstate Commerce

At the outset, there should be no doubt that the Colorado tax is inconsistent with the Commerce Clause. Petitioner demonstrates in detail that the tax should not survive application of the rule articulated in *Halliburton Oil Well Cementing Co.* v. *Reily*, 373 U.S. 64 (1963). See Pet. 10-13. Unsurprisingly, the tax also runs afoul of the broader principles that

animate this Court's Commerce Clause jurisprudence. The Court has understood the Clause to prevent states "from retreating into economic isolationism or jeopardizing the welfare of the Nation as a whole" (*Oklahoma Tax Comm'n* v. *Jefferson Lines*, 514 U.S. 175, 179-180 (1995)), either by directly discriminating against interstate commerce or by imposing taxes that more subtly "exert[] an inexorable hydraulic pressure on interstate businesses to ply their trade within the State that enacted the measure rather than 'among the several States.'" *American Trucking Associations, Inc.* v. *Scheiner*, 483 U.S. 266, 286-287 (1987) (quoting U.S. Const., Art. I, § 8, cl. 3). The Colorado tax does both.

The discriminatory impact of the tax is manifest. The amount of the levy turns on the price paid for the taxed product by the distributor who "first receives" the product in Colorado. As a consequence, it necessarily is the case that the amount of tax due will go up as more of the distribution chain is located outside Colorado, even if the products, packaging, marketing, and all other aspects of distribution are identical in every respect save location. There is no doubt about this effect of the tax. Indeed, the court below expressly acknowledged that "the location of the manufacturers, suppliers, or distributors involved in the product's distribution network and the price mark-up of each impacts the tax base or the price upon which the constant twenty percent tax rate is imposed" and "agree[d] with McLane's assertions that the tax base will be higher the later in the distribution network the product is taxed." Pet. App. 6a. The court accordingly agreed, as well, "that the tax base calculated on the price paid by the taxable distributor may place the product at a competitive disadvantage in the marketplace because the higher tax is added to the price." *Id.* at 8a. That effect casts grave doubt on the constitutionality of the tax: "Under [this Court's] consistent course of decisions in recent years a state tax that favors in-state business over out-of-state business for no other rea-

son than the location of its business is prohibited by the Commerce Clause." *Scheiner*, 483 U.S. at 286.

By the same token, taxes like Colorado's place "an inexorable hydraulic pressure on interstate businesses to ply their trade within the State that enacted the measure rather than 'among the several States.'" The court below denied that effect, declaring that "the OTP tax scheme does not pressure out-of-state businesses to move to Colorado." Pet. App. 10a. But the court gave no explanation for its conclusion, which plainly is wrong. After all, when the distribution network is entirely in one state the tax is lower than when otherwise identical distribution activities cross state lines. See *id.* at 6a. Such a regime "place[s] interstate commerce at a disadvantage as compared with commerce intrastate." *Jefferson Lines*, 514 U.S. at 185. Thus, "[a]s a practical matter, the statute encourages affected entities to limit their out-of-state" activities (*Camps Newfound/Owatonna, Inc.* v. *Town of Harrison*, 520 U.S. 564, 576 (1997)), which necessarily encourages "tendencies toward economic Balkanization." *Jefferson Lines*, 514 U.S. at 180 (citations and internal quotation marks omitted).

B. A State Tax That Discriminates Against Interstate Commerce In Its Practical Effect Is Inconsistent With The Commerce Clause

In nevertheless upholding the Colorado tax, the court below construed this Court's Commerce Clause decisions to establish that "a tax is discriminatory if it taxes out-of-state transactions or entities at a rate higher than it taxes in-state transactions, entities, or products, or if it exempts in-state transactions, entities, or products from an otherwise uniform tax." The court accordingly found it dispositive that "[a]ll taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion." *Id.* at App. 8a. This focus on the superficial form of the tax – and the com-

plete disregard for the practical consequences of the tax's discriminatory effects – was a serious error.

Although the court below placed crucial weight on the fact that the Colorado tax does not facially discriminate against out-of-state entities in its rate or exemptions, this Court has emphasized that "the Commerce Clause has a deeper meaning that may be implicated even though state provisions, such as the one[] reviewed here, do not allocate tax burdens between insiders and outsiders in a manner that is facially discriminatory." *Scheiner*, 483 U.S. at 281. In giving force to this "deeper meaning," the Court in its modern Commerce Clause decisions addressing state taxation has eschewed "a focus on * * * formalism [that] merely obscures the question whether the tax produces a forbidden effect." *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274, 288 (1977). Instead, in its "more recent decisions" the Court has "'moved toward a standard of permissibility of state taxation based upon its actual effect rather than its legal terminology.'" *Scheiner*, 483 U.S. at 294-295 (quoting *Complete Auto Transit*, 430 U.S. at 281). See, *e.g.*, *Jefferson Lines*, 514 U.S. at 183; *Commonwealth Edison Co.* v. *Montana*, 453 U.S. 609, 615 (1981).

Starting from this perspective, the Court's "cases have eschewed formalism for a sensitive, case-by-case analysis of purposes and effects." *West Lynn Creamery, Inc.* v. *Healy*, 512 U.S. 186, 201 (1994). This means that "'[w]hat is ultimate is the principle that one state in its dealings with another may not put itself in a position of economic isolation. Formulas and catchwords are subordinate to this overmastering requirement.'" *Id.* at 202 (quoting *Baldwin* v. *G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935)).

The Court has applied this principle repeatedly to invalidate state taxes that do not facially discriminate in their rates, exemptions, or tax bases, but that necessarily place interstate commerce at a competitive disadvantage. In *Nippert* v. *City*

of Richmond, 327 U.S. 416 (1946), for example, one of the seminal cases establishing the Court's modern Commerce Clause doctrine,[2] the Court struck down a flat municipal license fee imposed on solicitors (so-called "drummers") doing business in the city, explaining:

> [T]he tax * * * cannot be taken to apply generally to local distributors in the same manner and with like effects as in application to out-of-state distributors. The very difference in locations of their business headquarters, if any, and of their activities makes this impossible. This, of course, is but another way of saying that the very difference between interstate and local trade, taken in conjunction with the inherent character of the tax, makes equality of application between those two classes of commerce, generally speaking, impossible.

Id. at 432.[3]

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[2] The Court's opinion in *Nippert* was authored by Justice Rutledge, whose views anticipated the Court's modern Commerce Clause doctrine in significant respects and were substantially incorporated in the *Complete Auto Transit* test. See *Complete Auto Transit*, 430 U.S. at 280-281, 282

[3] The Court placed particular emphasis on the practical consequences of the challenged tax: "[The] tax imposes substantial excluding and discriminatory effects of its own. * * * [T]he small operator and especially the casual or occasional one from out of the State will find the tax not only burdensome but prohibitive, with the result that the commerce is stopped before it is begun. And this effect will be extended to more substantial and regular operators, particularly those whose * * * market in any single locality * * * cannot be mined more than once every so often." Such a tax thus "can easily mean the stoppage of a large amount of commerce which would be carried on either in the absence of the tax or under the incidence of one taking account of those variations." *Id.* "Whether or not it was so intended, those are [the flat tax's] necessary effects." *Id.* at 434.

The Court applied this same principle to invalidate flat taxes on interstate motor carriers in *Scheiner*. Although the levies were "facially neutral" (483 U.S. at 269), the Court recognized that the challenged taxes necessarily disadvantaged interstate businesses: "[T]he very nature of the market that interstate operators serve prevents them from making full use of the privilege * * * for which they have paid the State" a flat fee. *Id.* at 284 n.16. Thus,

> "the intrastate vehicle can and will exercise the privilege whenever it is in operation, while the interstate vehicle must necessarily forego [*sic*] the privilege some of the time simply because of its interstate character, i.e., because it operates in other States as well. In the general average of instances, the privilege is not as valuable to the interstate as to the intrastate carrier."

Id. at 291 (quoting *Capitol Greyhound Lines* v. *Brice*, 339 U.S. 542, 557 (1950) (Frankfurter, J., dissenting)).

Similarly, in *Baldwin* v. *G.A.F. Seelig*, *supra*, the Court held dispositive the practical effect of a facially neutral levy. There, New York established a uniform, minimum price for all milk, wherever produced. But "[t]his Court * * * did not hesitate to strike [the tax] down." *West Lynn Creamery*, 512 U.S. at 193. Writing for the Court, Justice Cardozo explained:

> Neither the power to tax nor the police power may be used by the state of destination with the aim and effect of establishing an economic barrier against competition with the products of another state or the labor of its residents. Restrictions so contrived are an unreasonable clog upon the mobility of commerce. They set up what is equivalent to a rampart of customs duties designed to neutralize advantages belonging to the place of origin.

294 U.S. at 527. As the Court subsequently described *Baldwin*, "because the minimum price regulation had the same

effect as a tariff or customs duty – neutralizing the advantage possessed by lower cost out-of-state producers – it was held unconstitutional." *West Lynn Creamery*, 512 U.S. at 194. See also, *e.g.*, *Hunt* v. *Washington State Apple Advertising Comm'n*, 432 U.S. 333, 352-353 (1977); *Dean Milk* v. *Madison*, 340 U.S. 349 354 (1951); *Best & Co.* v. *Maxwell*, 311 U.S. 454, 455-456 (1940).

In all of these cases, the challenged taxes – like the Colorado levy – gave the appearance of equality. Like the Colorado tax, none of the challenged levies "tax[ed] out-of-state transactions or entities at a rate higher than it taxe[d] in-state transactions, entities, or products, or * * * exempt[ed] in-state transactions, entities, or products from an otherwise uniform tax." Pet. App. 7a. Yet this Court invalidated them all because they were structured so that their practical effects placed interstate commerce at a disadvantage as compared to otherwise identical commerce conducted exclusively in one state. Precisely the same conclusion is warranted here: as was true of the levy invalidated in *Nippert*, the Colorado tax "cannot be taken to apply generally to local distributors in the same manner and with like effects as in application to out-of-state distributors."327 U.S. at 432.

C. The Court Should Grant Review To Clarify The Proper Treatment Of State Taxes That Discriminate Against Interstate Commerce In Their Practical Effect

The fundamental question presented here – how courts should approach state taxes that are facially neutral but discriminate against interstate commerce in their practical effect – is an important and recurring one that warrants this Court's review. It is an unfortunate reality that states have never stopped experimenting with taxes that place subtle but significant burdens on businesses that operate across state lines. Express discrimination is rare; "[i]n fact, tariffs against the products of other states are so patently unconstitutional that

[the Court's] cases reveal not a single attempt by any State to enact one. Instead, the cases are filled with state laws that aspire to reap some of the benefits of tariffs by other means." *West Lynn Creamery*, 512 U.S. at 193.

There is no mystery about the reason for the perennial nature of such state enactments. The practical burden of truly evenhanded state taxes "'usually falls on local economic interests as well as other States' economic interests, thus insuring that a State's own political processes will serve as a check against unduly burdensome regulations.'" *West Lynn Creamery*, 512 U.S. at 200 (quoting *Raymond Motor Tranport, Inc.* v. *Rice*, 434 U.S. 429, 444 n. 18 (1978)). But there is no in-state political constituency to curtail the enactment of tax regimes that disproportionately burden out-of-state taxpayers. To the contrary, every state has an understandable incentive to export as much of its tax burden as possible to foreign entities – a course that has the added benefit (from the enacting state's perspective) of providing a competitive advantage to businesses that concentrate their operations in the taxing state.

ATA's experience demonstrates this reality. Following this Court's landmark *Scheiner* decision in 1987, which held that flat state taxes on interstate motor carriers violate the Commerce Clause, ATA hoped that states would recognize the decision's unequivocal condemnation of flat, annual charges on interstate trucking operations and quickly eliminate them. Instead, most states tried to evade *Scheiner*'s principles and forced ATA to undertake an ongoing, decades-long litigation effort to enforce the Commerce Clause requirements that *Scheiner* articulated. See, *e.g.*, *Commonwealth Transportation Cabinet* v. *American Trucking Associations, Inc.*, 746 S.W. 2d 65 (Ky. 1988); *Black Beauty Trucking, Inc.* v. *Indiana Dept. of Revenue*, 527 N.E. 2d 1163 (Ind. Tax Ct. 1988); *American Trucking Associations, Inc.* v. *Secretary of State*, 595 A.2d 1014 (Me. 1991); *American Trucking Associations, Inc.* v. *State*, 556 N.W. 2d 761 (Wis.

Ct. App. 1996), rev. denied, 560 N.W.2d 274 (Wis. 1996). All told, ATA has been forced to bring suit against 15 states challenging more than two dozen flat state taxes and fees imposed on interstate trucking.[4] Indeed, that effort continues to

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[4] *American Trucking Associations, Inc.* v. *State of New Jersey*, 852 A.2d 152 (N.J. 2004) (hazardous waste transporter fee (N.J. Stat. Ann. § 13:1E-18)); *American Trucking Associations, Inc.* v. *State*, 556 N.W. 2d 761 (Wis. Ct. App. 1996), rev. denied, 560 N.W.2d 274 (Wisc. 1996) ($400-per-company hazardous material transportation fee (Wis. Admin. Code § SERB 4.03(2)(a)-(e)); *American Trucking Associations, Inc.* v. *New Hampshire*, No. 89-E-00405-B (N.H. Super. Ct., Merrimack Co., 1995) ($200-per-unit hazardous waste transporter fee (N.H. Rev. Stat. Ann. § 147-A:6, II) and $25-per-unit hazardous material fee (reduced to $5-per-truck during the litigation) (N.H. Rev. Stat. Ann. § 21-P:20, IV)); *American Trucking Associations, Inc.* v. *Denn*, No. C2-95-4910 (Minn. Dist. Ct., Ramsey Cty., 1995) ($40-per-vehicle cab card fee (Minn. Stat. § 221.31)); *American Trucking Associations, Inc.* v. *Secretary of Admin.*, 613 N.E. 2d 95 (Mass. 1993) ($7-per-truck license fee and $7-per-truck "user of special fuels" license fee (Mass. Gen. Laws ch. 62C, § 67) and $200-per-truck hazardous waste carrier fee (Mass. Gen. Laws ch. 21C, § 7)); *American Trucking Associations, Inc.* v. *Smith*, No. 89-0385 (Ark. Chancery Ct., 1992) ($10-per-truck fuel decal tax (Ark. Code Ann. § 26-55-708 (2)); *American Trucking Associations, Inc.* v. *Cowan*, No.TX91-01608 (Ariz. Chancery Ct., 1992) ($125-per-truck cargo tank fee (Ariz. Rev. Stat. § 28-3005) and $100-per-carrier, $25-per-truck hazardous and special waste transporter fees (Ariz. Rev. Stat. §§ 28-2421 and 28-2422)); *Marx* v. *American Trucking Associations, Inc.*, 600 So. 2d 212 (Miss. 1992) ($12-per-truck fuel identification fee (Miss. Code Ann. § 27-61-5(1)) and $13-per-truck bingo stamp fee (Miss. Code Ann. § 77-7-119)); *American Trucking Associations, Inc.* v. *Secretary of State*, 595 A.2d 1014 (Me. 1991) ($25-per-truck hazardous waste fee (Me. Rev. Stat. Ann. tit. 29 § 246-D)); *American Trucking Associations, Inc.* v. *New Hampshire*, No. 89-E-00405 (N.H. Super. Ct., Merrimack Co., 1991) ($20-per-truck decal fee (N.H. Rev. Stat. Ann. § 260:52, V (Supp. 1988))); *American Trucking Associations, Inc.* v. *Secretary of State*, No. CV-89-410 (Me.

this day: ATA's challenge to Oregon's flat motor carrier tax, which was successful in the Oregon Court of Appeals but rejected by the Oregon Supreme Court, is now pending in this Court. See No. 05-1177, *American Trucking Associations, Inc.* v. *State of Oregon* (cert. pending) (challenging *American Trucking Associations, Inc.* v. *State of Oregon*, 124 P. 3d 1210 (Or. 2005)).

Although interstate motor carriers have been a particular target of parochial state taxation, all businesses that operate across state lines are potential victims of taxes that have a discriminatory impact on interstate commerce. This Court's decisions, which over the years have resolved Commerce Clause challenges brought by taxpayers in virtually all industries and sectors of the economy, illustrate that point graphically. See, *e.g.*, *West Lynn Creamery*, 512 U.S. at 194 (citing cases). Yet, as the decision below shows, the lower courts continue to struggle with the principles that govern "practical effects" discrimination.

1990) ($15-per-truck decal fee (Me. Rev. Stat. Ann. tit. 29 § 246-A)); *American Trucking Associations, Inc.* v. *Conway*, 566 A.2d 1323 (Vt. 1989) ($50-per-truck fuel decal fee (Vt. Stat. Ann. tit. 23 § 415 (1982)) and $50-per-truck retaliatory fee (Vt. Stat. Ann. tit. 23 § 3007 (1982))); *American Trucking Associations, Inc.* v. *Goldstein*, 541 A.2d 955 (Md. 1988) ($25-per-truck fuel decal fee (Md. Ann. Code art. 81, § 423(a)(1987 Cum. Supp.)); *Commonwealth Transportation Cabinet* v. *American Trucking Associations, Inc.*, 746 S.W.2d 65 (Ky. 1988) ($150-per-truck supplemental highway use tax (Ky. Rev. Stat. Ann. § 1388.660(4-7)); *American Trucking Associations, Inc.* v. *Gray*, 746 S.W.2d 377 (Ark. 1988) ($175-per-truck highway use equalization tax (Ark. Code. Ann. §§ 75-817 and 75-819)); *Black Beauty Trucking, Inc.* v. *Indiana Dept. of Revenue*, 527 N.E.2d 1163 (Ind.Tax Ct., 1988) ($50-per-truck supplemental highway use tax (Ind. Code § 6-6-8-1 et seq.)); *American Trucking Associations, Inc.* v. *Kline*, 9 N.J.Tax 631 (N.J., 1987) ($25-per-truck fuel decal fee (N.J. Stat. Ann. § 54:39A-10)).

This issue involves a matter of tremendous importance to the national economy. As the Court has observed repeatedly, the values embodied in the Commerce Clause "reflect a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation." *Jefferson Lines*, 514 U.S. at 180 (citations and internal quotation marks omitted). See, *e.g.*, *Oregon Waste Sys., Inc.* v. *Dep't of Envtl. Quality*, 511 U.S. 93, 98 (1994).

Thus, as ATA emphasizes in its own pending petition for certiorari in No. 05-1177, *American Trucking Associations, Inc.* v. *State of Oregon*, whether or not "the facts of this particular case, viewed in isolation, * * * appear to pose any threat to the health of the national economy," the aggregate effect of statutes like these cannot be gainsaid:

> [H]istory, including the history of commercial conflict that preceded the constitutional convention as well as the uniform course of Commerce Clause jurisprudence animated and enlightened by that early history, provides the context in which each individual controversy must be judged. The history of [the Court's] Commerce Clause jurisprudence has shown that even the smallest scale discrimination can interfere with the project of our federal Union. As Justice Cardozo recognized, to countenance discrimination of the sort that [Colorado's] statute represents would invite significant inroads on our "national solidarity."

Camps Newfound/Owatonna, 520 U.S. at 595 (quoting *Baldwin*, 294 U.S. at 523). In light of this important principle, the Court has acknowledged its "'duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against in-

terstate commerce.'" *West Lynn Creamery*, 512 U.S. at 201 (quoting *Best & Co.*, 311 U.S. at 455-456). Because the Colorado tax is structured to work such a practical discrimination, because discriminatory state taxes of this sort regularly pop up to bedevil taxpayers across the country, and because the proper treatment of such taxes continues to confuse state courts, this Court should grant review.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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In The Supreme Court of the United States

MCLANE WESTERN, INC.,

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v.

DEPARTMENT OF REVENUE, STATE OF COLORADO, *ET AL.*,

Respondents.

On Petition For Writ Of Certiorari To The Colorado Court Of Appeals Division IV

BRIEF OF THE COLORADO ASSOCIATION OF DISTRIBUTORS AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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INTEREST OF *AMICUS CURIAE*

This *amicus curiae* brief in support of the brief of Petitioner is submitted pursuant to Rule 37 of the Supreme Court Rules.[1] Counsel for Petitioner and Respondents have consented to the filing of this brief. Their consent letters have been filed with the Clerk of the Court.

The Colorado Association of Distributors ("the Association") is a federation of eight companies[2] engaged in the distribution and wholesale sale of cigarettes and other tobacco products, confections, snacks, health and beauty care products, and assorted other items. The Association works to protect and promote the interests of its members in dealings with manufacturers, distributors, retailers, and the public at large.

All of the Association's members, like Petitioner, purchase tobacco products other than cigarettes from distributors located outside Colorado. As a consequence, Association members acquire tobacco products following sales (and associated price mark-ups) that take place wholly outside Colorado. Because the base for the subject levy is the price paid by the distributor that first brings or ships the tobacco products into the state, Association members either pay directly to the State of Colorado or find embedded within their purchase price a higher tax

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[1] Pursuant to Supreme Court Rule 37.6, counsel for *amicus curiae* state that no counsel for any party authored this brief in whole or in part and that no entity other than *amicus curiae* made a monetary contribution to the preparation or submission of this brief.

[2] The eight companies are: Bradford Distributing, Cash-Wa Distributing, Cigarette Store Corporation, Core-Mark International, Creager Mercantile, McLane Western, Inc., Smoker Friendly International, and S.R. Flaks Company.

than they would pay were the tobacco products manufactured or first distributed within Colorado. Thus, *amicus curiae* and its members are directly impacted by the levy's discrimination against interstate commerce.

SUMMARY OF THE ARGUMENT

Amicus curiae makes three points in this brief. First, the Colorado tax on tobacco products other than cigarettes produces genuine economic harm for distributors, such as the Association's members, that choose to do business with out-of-state entities. Because the ultimate Colorado tax base rises with each sale taking place outside the state, Colorado distributors face a higher tax burden (and therefore, inevitably, higher product prices) the later in the stream of commerce the tobacco products enter the state. These higher prices both reduce demand for the product and place distributors that acquire product through out-of-state channels at a competitive disadvantage versus those distributors that elect or are able to acquire product that enters Colorado earlier in the stream of commerce.

Second, these effective penalties upon participation in the interstate market for goods have a coercive effect on economic decision-making. The Colorado scheme pressures Colorado distributors to prefer and to seek Colorado sources for acquiring tobacco products. At the same time, it pressures out-of-state manufacturers and distributors to relocate operations into Colorado (so as to satisfy Colorado distributors' interest in minimizing the tax base). These pressures are real, and they are material.

Third, the principles raised by this matter are far-reaching. If the Colorado levy on tobacco products is allowed to stand, virtually any excise tax on virtually any product could be molded to prefer in-state activities at the expense of out-of-state activities.

ARGUMENT

I. THE COLORADO TAXING SCHEME BROADLY DISCRIMINATES AGAINST DISTRIBUTORS THAT ACQUIRE OTHER TOBACCO PRODUCTS FROM OUT-OF-STATE CHANNELS

As a factual matter, it cannot reasonably be disputed that the Colorado scheme imposes a higher levy on tobacco products first marketed and distributed through out-of-state channels than it imposes on products immediately marketed and distributed within Colorado. By setting the tax base as the prevailing product price upon the occurrence of the first of various enumerated events that takes place "in this state," the Colorado statute ensures that commerce conducted outside the state will suffer a heavier burden than commerce conducted within the state. *See* Colo. Rev. Stat. § 39-28.5-102 (identifying events that trigger the levy); *see also id.*, § 39-28.5-101(3) (defining "manufacturer's list price").

Petitioner has presented effectively the legal authorities that mark this scheme constitutionally infirm (*see* Petition for Writ of Certiorari ("Petition"), pp. 9-19), and accordingly, *amicus curiae* does not repeat that discussion here. Instead, *amicus curiae* wishes to highlight the very significant and widely-felt impact of the present discrimination. *Any* Colorado distributor that relies upon out-of-state

channels to acquire tobacco products will face a higher levy on the products than it would face if it relied on in-state channels.

The nature of the tobacco products industry is such that virtually all manufacturing activity takes place outside Colorado. Moreover, product often passes from the manufacturer through one or more distributors before reaching Colorado. Indeed, most of the Association's members purchase tobacco products following out-of-state sales. Because each out-of-state sale has the effect of inflating the ultimate tax base, virtually all tobacco products that reach the state will experience a heightened levy based solely on the locus of earlier commercial activity outside the state. Given that the tax is now imposed at a rate of 40% of the product price upon entry into Colorado (*see* Colo. Rev. Stat. §§ 39-28.5-102, 39-28.5-102.5), virtually any increase in the tax base will generate a material increase in the tax due.

These higher levies have direct consequences for Colorado distributors of tobacco products. They necessarily translate into either higher downstream prices (and a consequent reduction in sales) or lower product margins, or a combination of both. At the same time, the disparate burden on non-Colorado commerce leaves many Colorado distributors, including the members of *amicus curiae*, at risk of competition from other distributors whose only advantage is an ability to acquire tobacco products that enters the state earlier in the stream of commerce.[3]

[3] *Amicus curiae* notes that these same pressures and competitive threats may be felt by retailers that acquire tobacco products following predominantly non-Colorado commerce.

Amicus curiae believes that industry participants should not be penalized due to decisions to conduct business with entities operating outside Colorado.

II. THE COLORADO TAXING SCHEME PRECLUDES GEOGRAPHICALLY-NEUTRAL DECISION-MAKING AND INVITES IRRATIONAL BEHAVIOR

If allowed to stand, all Colorado distributors that rely on out-of-state distribution channels (including all of *amicus curiae*) will be heavily incented to pursue new product sources that are able to bring the product to Colorado earlier in the stream of commerce. For example, in-state, upstream distributors will be preferred over out-of-state, upstream distributors. Conversely, entities now operating entirely outside Colorado will need to consider relocating operations into Colorado in order to meet customers' demand for a lower levy, and hence, a lower product price.

While the behavior induced by this scheme may reduce the levy itself, it is otherwise economically irrational. Consider a first-level distributor ("D1") that currently purchases tobacco products from a manufacturer entirely outside Colorado, but then re-sells that same product, at a marked-up price, to a second-tier distributor ("D2") operating in Colorado. Under Colorado's current scheme, the marked-up price paid in the second sale will set the base for the levy, as it is this second sale that causes the product to enter the state. As a result, D1 now has a choice. D1 may continue business as usual, leaving D2 to pay tax on a higher base. Or, D1 may establish a warehouse in Colorado and have the manufacturer ship all product D1 intends to sell to D2 to the Colorado warehouse.

Choosing this latter option (*i.e.*, routing the product to Colorado prior to the sale to D2) will reduce the tax base from the price D2 pays D1 to the price D1 pays the manufacturer, thus reducing the ultimate product cost to D2. Yet, in chasing this lower tax base, D1 has established a warehouse in Colorado that serves no other economic purpose. To the contrary, it very likely creates substantial additional burdens. Now consider how these burdens would be magnified if every state established its tax base in the same manner as Colorado.

III. VALIDATION OF THE COLORADO METHODOLOGY HAS BROAD RAMIFICATIONS FOR OTHER EXCISE TAXES

Colorado might have chosen any number of alternative methodologies for determining its tax base that would not have discriminated against interstate commerce. Colorado could have measured the tax base by the price charged to the ultimate consumer, as, for example, a traditional sales tax. The state could have measured the tax base by the units of product sold, as, for example, per-gallon excise taxes on fuel. Or, Colorado could have measured the tax base by the weight of the product sold, as, for example, per-ounce excise taxes on tobacco products. Each of these other methodologies, in contrast to Colorado's, makes no distinction regarding where events in the stream of commerce take place, and accordingly, each raises no constitutional concern.

Validation of Colorado's scheme by the Court would expose an array of other excise taxes to a similar preference for in-state activities. For example, if the Colorado levy on tobacco products were allowed to stand, Colorado (or any other state) could modify its sales tax to measure

the tax base for the sale of any item of tangible personal property by the price paid upon the first sale by a manufacturer or distributor within the state. In this manner, virtually every product sold would face differential taxes depending on the level of commercial activities that took place with respect to that product within or without the taxing state. The widget manufactured and first distributed outside Colorado would face a higher tax than the widget manufactured and first distributed within Colorado. Again, the result would be to coerce in-state operations (*e.g.*, manufacturing and distribution) at the expense of out-of-state activities. Such discrimination against interstate commerce does violence to our national market for goods, and *amicus curiae* urges the Court to declare it unconstitutional.

CONCLUSION

For the foregoing reasons, and those set forth in the brief of Petitioner, the Court should grant the Petition and reverse the Colorado Court of Appeals.

Respectfully submitted,

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BRIEF OF *AMICI CURIAE* COUNCIL ON STATE TAXATION, THE NATIONAL ASSOCIATION OF WHOLESALER DISTRIBUTORS, AND THE NATIONAL ASSOCIATION OF MANUFACTURERS IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether the Colorado excise tax, which varies based on whether the underlying economic activity occurs in-state or out-of-state, violates the Commerce Clause of the Constitution, U.S. Const. Art. I, § 8, cl.3.

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BRIEF OF *AMICI CURIAE* COUNCIL ON STATE TAXATION, THE NATIONAL ASSOCIATION OF WHOLESALER DISTRIBUTORS, AND THE NATIONAL ASSOCIATION OF MANUFACTURERS IN SUPPORT OF PETITIONERS

This brief is filed, with the written consent of the parties lodged with the Clerk of this Court, on behalf of the Council On State Taxation, the National Association of Wholesaler Distributors, and the National Association of Manufacturers as *amici curiae* in support of petitioner. Between the three *amici curiae* that have joined to file this brief, every major industry is represented.[1]

[1] No counsel for a party authored this brief in whole or in part, and no person or entity, other than *amici curiae*, has made a monetary contribution to the preparation or submission of this brief. Written consent of all parties have been obtained and filed with the Clerk of the Court.

INTEREST OF *AMICI CURIAE*

Description of Associations Filing as Amici

The Council On State Taxation ("COST"), is a non-profit trade association formed in 1969 to preserve and promote equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. COST represents nearly 600 of the largest corporations in the United States, including companies from every industry segment. COST's membership conducts business in every state and between every state. The membership pay tax in every state and are concerned when states or localities seek to circumvent this Court's application of Constitutional limitations on their ability to discriminate against interstate commerce. COST's mission is to preserve and promote equitable and nondiscriminatory taxation of multistate businesses. Thus, COST members, and the organization itself have a financial and organizational interest in whether the Colorado excise tax is unconstitutional.

The National Association of Wholesaler-Distributors ("NAW") is a non-profit trade association that represents the wholesale distribution industry. NAW is comprised of direct member companies and a federation of more than 100 national, regional, state and local associations and their member firms which, collectively, total approximately 40,000 companies operating at some 150,000 locations throughout the nation. NAW's members are a constituency at the core of the U.S. economy—the link in the marketing chain between manufacturers and retailers as well as commercial, institutional and governmental end-users. While industry firms vary widely in size, wholesaler-distributors generally are small to medium-size, closely-held businesses providing stable, well-paying jobs to more than 5 million Americans and account for some $3.6 trillion in annual economic activity in 2005. Nearly all of NAW's members are engaged in interstate commerce, and thus even those members who are not directly affected by the Colorado excise tax at issue, will

benefit from, and are entitled to, the positive business environment ensured by the Commerce Clause of the United States Constitution.

The National Association of Manufacturers ("NAM") is the nation's largest industrial trade association, representing small and large manufacturers in every industrial sector and in all 50 states. NAM's mission is to enhance the competitiveness of manufacturers by shaping a legislative and regulatory environment conducive to U.S. economic growth and to increase understanding among policymakers, the media and the general public about the vital role of manufacturing to America's economic future and living standards. The members of NAM thus also have a financial interest in whether the Commerce Clause protects its members from discriminatory taxation by the states.

Description of Amici Interest

While the particular tax at issue in this case is a narrow excise tax applicable only to the distribution of tobacco products other than cigarettes, the decision of the Colorado Court of Appeals could affect a far broader range of taxes and taxpayers if its rationale is allowed to stand. The Colorado court's decision in this case, if left unchecked, provides a roadmap for discrimination against interstate commerce for practically all methods of state and local taxation. It is this risk of application beyond the specific tax at issue that has caused significant concerns for the *amici* and motivated the *amici's* contribution to this case. *Amici*, as national organizations, have a unique perspective on the wider applications and implications that the reasoning by the Colorado court could have on other industries, other taxpayers, other tax regimes, and other state and local governments. *Amici* also seek to bring to this Court's attention the importance of resolving this issue before it spreads. It has been the unfortunate experience of *amici* and *amici's* members that many states have a significant reluctance in remedying unconstitutional taxes. Because

of *amici's* experience with this historical reluctance, *amici* have an interest in seeing this issue resolved expeditiously. In sum, *amici* have both an interest in this case to prevent stealth discrimination against interstate commerce from proliferating and a national and multi-industry expertise to discuss relevant matter not already brought to this Court's attention by the parties.

SUMMARY OF ARGUMENT

The Colorado excise tax unconstitutionally varies based on whether the underlying economic activity occurs in-state or out-of-state. As products subject to the tax move from manufacturing to retail sale, the Colorado tax increases in amount if these processes take place outside the state but not if the processes take place in the state. By structuring the tax to apply when the product enters the state (as opposed to a tax on unit, weight, value or on the ultimate sales price as is done in innumerable other tax structures) Colorado has created a tax that discriminates against interstate commerce while appearing facially neutral.

Unchecked, the Colorado Court of Appeals' decision provides a ready roadmap for states to convert constitutional taxes into taxes that discriminate against interstate commerce. Further, even taxes found unconstitutional by this court and others could be revived using the Colorado model. In either case the decision gives a blueprint for states to impose a tax burden on interstate commerce without imposing the same burden on their own.

Lastly, delay in resolving this issue will inevitably lead to an unnecessary financial crisis for state governments and exponential growth of the illegal tax on interstate commerce. A denial of certiorari in this case will encourage states to rely on an unproven and suspect tax structure which, if eventually reviewed by the U.S. Supreme Court, should be struck down as unconstitutional. Delaying what *amici* believes to be in-

evitable will expose state tax receipts to claims for refund and thus create uncertainty for taxpayers and state government alike. In a very real way the Court has the ability to prevent the roof from falling in before state governments build their houses on unstable grounds.

ARGUMENT

I. Under the Commerce Clause of the United States Constitution, the Colorado excise tax unconstitutionally discriminates against interstate commerce because the net result of the tax regime is a higher tax on items purchased from manufacturers, wholesalers, and distributors located outside of Colorado than the tax on items purchased from such businesses operating within Colorado.

The question presented in this appeal is whether the Colorado excise tax, which varies based on whether the underlying economic activity takes place in-state or out-of-state, violates the Commerce Clause of the Constitution, U.S. Const. Art. I, § 8, cl.3. The ramifications of this appeal however, are not limited to the tax type, tax jurisdiction, or taxpayer involved. Because the decision below creates a roadmap for discrimination it is critical that the U.S. Supreme Court review the tax structure before it is adopted by other states to in an effort to export their tax burden. Such review will help minimize fiscal disruption and uncertainty for states and taxpayers alike.

Colorado's excise tax violates the Commerce Clause because its impact is to impose a greater tax on products manufactured and distributed from out-of-state than it does on products manufactured and distributed in-state. Decades of U.S. Supreme Court precedent, including *Fulton Corp. v. Faulkner*, 516 U.S. 325 (1996), hold that under the Commerce Clause a state may not discriminate in its tax system in favor of local companies over out-of-state companies.

The Commerce Clause of the United States constitution provides that Congress shall have the authority to "regulate commerce . . . among the several states." Art. I, §8, cl. 3. This affirmative grant of power has given rise to a concomitant negative or dormant implication—the states may not discriminate against interstate trade. *Associated Industries v. Lohman*, 511 U.S. 641, 646 (1994). The dormant element of the Commerce Clause thus prohibits economic protectionism on the part of states. States may not adopt measures designed to benefit in-state economic interests by burdening out-of-state competitors. *Id.* at 647. Thus, a state may not tax a transaction or incident more heavily when it crosses states lines than if it were to occur entirely within one state. *Id.* Economic protectionism can be made out by a showing of either discriminatory effect or discriminatory intent. *Bacchus Imports Ltd. v Dias*, 468 U.S. 263, 270 (1984).

Petitioner McLane is indeed subject to a greater tax burden by Colorado as a direct result of its interstate trade. The tax at issue here is an example of a violation of the Commerce Clause through a discriminatory effect instead of a discriminatory purpose. Petitioner is a distributor of smokeless tobacco products within Colorado known as OTP ("other tobacco products"). Petitioner buys OTP from an out-of-state distributor and then resells the products in-state. The Colorado tax at issue in this case is an excise tax that is imposed on the sale, use, consumption, handling, or distribution in the state of all OTP tobacco products. Colo. Rev. Stat. §39-28.5-102(1). However, the tax is imposed once and only once on the first Colorado distributor, which means the first distributor in Colorado to receive the OTP. *Id.*

The crux of this case, and the reason that the excise tax is clearly invalid, lies with the fact that the more activity that occurs in the distribution chain of the OTP *outside* of Colorado the higher the cost of the OTP due to mark-ups. Thus, a higher tax base leads to a higher eventual tax paid by

Petitioner. If the entire distribution chain were located *inside* of Colorado, the same combined excise tax would be owed by the original manufacturer (here UST Manufacturing), but would be owed on a much smaller tax base because the tax is calculated earlier in the distribution chain. This is called a 'shifting tax base' because the amount included within the tax base depends on when the product enters the state.

The end result of the Colorado tax, and the Colorado Court of Appeals interpretation of it, is to discriminate against inter-state commerce in favor of intra-state (i.e. Colorado only) commerce. This violates the Commerce Clause and the Supreme Court's decision striking down discrimination based on a shifting tax base in *Halliburton*. *Halliburton Oil Well Cementing Co. v. Riley*, 373 U.S. 64 (1963). The ruling on the Colorado tax is especially pernicious because it could just as easily apply to any sort of state tax. For instance, sales, use, income, property, and excise taxes could each be reconfigured based on the Colorado court's rationale.

If the analysis of the Colorado court is acceptable, any state wishing to give a discriminatory boost to its in-state companies could simply switch its tax base to one which depends on when the good or activity taxed first occurs in the state. For example—the sales tax is a widely adopted transaction tax imposed on the final sale to the ultimate consumer of tangible personal property (and some services). Typically, the sales tax is collected by the retail vendor but paid by the vendor's customer. It would clearly be unconstitutional for a state to impose a higher sales tax rate on items manufactured in other states than items manufactured in the taxing state (e.g. a 5% rate for non-Colorado manufactured goods and a 1% rate for Colorado goods). However, under Colorado's theory of the Commerce Clause, a switch in the collection point for a sales tax could accomplish just such a rate differential. If a state imposed the sales tax not on the *final sale* but instead on the *first sale that occurred within the state* but still provided that

the tax would be passed through and paid by the ultimate consumer, the tax would be "constitutional" under the Colorado court's analysis but clearly unconstitutional under this Court's Commerce Clause jurisprudence because it achieves the same result as imposing a higher tax rate on goods manufactured out of state.

The practical (and unconstitutional) result of taxing goods manufactured out of state more than goods manufactured in state in this hypothetical occurs because of the economic reality that sales prices increase throughout the taxable good's distribution chain from manufacturer, through wholesalers and distributors, to the final retailer and customer since each stage of the distribution chain adds value and requires a profit. As an example, assume a manufacturer sells to a distributor a product for $100; the distributor will sell that good to a wholesaler for $110; the wholesaler will sell the good to a retailer for $120; and the retailer will sell the good to the final customer for $150. Further, assume a hypothetical tax rate of 10%. Thus, under the hypothetical tax imposed on the first sale in the state as described above, if the manufacturer of a taxable good is in the taxing state, the first sale of that taxable good would occur when that manufacturer sold the product to a wholesaler, retailer, or other distributor. This price would in almost all cases be less than the final retail price. In our example, the taxable price would be $100 and the tax on such a sale would be $10 ($100 tax base x 10% tax rate). Under the hypothetical tax, that tax would be added to each subsequent receipt until ultimately paid by the final consumer. However, for an out-of-state manufacturer, wholesaler, distributor, and retailer selling goods at the same price, the tax passed through to the final customer will be much higher. If all elements of the distribution chain take place outside of the state except for the final sale by the retailer to the customer ($150 sales price in our example) then the first sale occurring in the state will be that final sale to the ultimate customer. At a tax base of $150, even with an allegedly non-

discriminatory 10% tax rate, the customer purchasing goods made and sold out of state will pay a sales tax of $15 as opposed to the tax of $10 if the manufacture and distribution activities had occurred in the state. Thus, from the customer's, and actual taxpayer's, point of view, the transaction and the product are exactly the same but the final tax is drastically different. Economically, the result is exactly the same as if the state had imposed a typical sales tax on the final sales price but imposed a tax rate of 10% for locally manufactured goods but 15% for goods from other states. This creates a significant incentive for retailers to purchase from in-state companies from which the tax has already attached—a classic sign of a tax which discriminates against interstate commerce.

If this hypothetical sales tax example is not enough to convince this Court of the very real risk of the widespread discrimination potential of the Colorado court's ruling, another potential scenario can also be posited. The Colorado tax at issue is really no different from a retail tobacco tax with a tax credit to tobacco retailers purchasing products from in-state manufacturers and distributors. If the Colorado tobacco tax were imposed not on the first use in the state but instead on all retail sales in the state, the tax base would be the same for all tobacco purchases. If a tax credit were provided to retailers buying from local manufacturers for the tax on the difference between the manufacturer's sales price and the final retail sales tax, the financial result and burden of the tax would be exactly the same as Colorado's current scheme. However, it seems abundantly clear that a tax credit only for purchases from in-state manufacturers/distributors would violate the discrimination prong of the Commerce Clause. If the Colorado court's opinion is allowed to stand, states will be able to achieve the equivalent of an unconstitutional tax credit for purchases from in-state manufacturers, except that the states will have to go through the inefficient hoops blessed by Colorado. The result is both a tax that unconstitutionally

discriminates against interstate commerce and a very complicated and inefficient tax imposition system.

II. The Potential Reach of the Colorado Court's Analysis and Past Experience With States' Inability or Unwillingness to Promptly and Completely Remedy Discriminatory Taxes Suggest that It is Prudent for This Court To Promptly Address the Issue.

While for many sensible and judicious reasons, this Court is cautious in accepting cases for which there has not been significant attention given by several other courts, it is important that the Court act now in this matter to forestall problems that might arise if the States, after enacting a broad but discriminatory tax following Colorado's model, must ultimately eliminate the tax after it is struck down by this or some other court. The risk of future problems, both for states and taxpayers, is not mere fear-mongering but is based on painful and frustrating past experience. State legislatures enact unconstitutional taxes for as many reasons as there are state legislators. Whether because of time constraints, budget limitations, misunderstanding, or willful disregard, state legislatures have always and appear to continue to enact tax statutes that unconstitutionally discriminate against interstate commerce. The real problem occurs, however, in the states' failure and inability to properly and fully grant real relief to taxpayers that suffer real economic injuries from such discrimination once the unconstitutionality of the action is pointed out by a judicial authority. States use many devices to delay, sometimes, indefinitely, the day of reckoning. Delay itself can frequently deny an injured taxpayer a true remedy.

It is not just taxpayers that can be injured by a delay in determining whether a tax is unconstitutional. States rely on the revenue stream from the taxes assessed and on the books. States are required to maintain a balanced budget each year so

any shortfall must be accommodated quickly and fully. While states can offer a variety of remedies to aggrieved taxpayers to avoid financial crisis in the budget—such as tax credits in lieu of refunds, installment refunds, and pre-deprivation hearing opportunity—each of these alternatives still affects the state fisc. The longer the validity of a tax remains uncertain, the larger the problem the state budget will have to bear should the tax ultimately be found unconstitutional.

The *South Central Bell* case is the most recent and a most frustrating example of the inability of taxpayers to obtain timely and thus adequate remedies for an unconstitutional tax. *South Central Telephone Co. v. Alabama*, 526 U.S. 160 (1999) (question of proper remedy still pending seven years after tax found unconstitutional). This Court ruled in 1999, with no opposition on the merits from the state of Alabama, that Alabama's corporate franchise tax, which had been in existence for approximately 100 years, was unconstitutional as it discriminated against interstate commerce. This Court accepted this case only after denying review of an earlier case on the same issue. Unfortunately for both Alabama and Alabama corporate franchise tax taxpayers, Alabama's budget has not been able to absorb the sheer number of claims for refund (once estimated to equal the entire annual budget of the state) following this Court's invalidation of the tax. As a result, Alabama has never provided full refunds to aggrieved taxpayers. Instead, Alabama has pursued various judicial arguments as to why refunds are not required (notwithstanding its apparent admission in this Court that its tax was unconstitutional) and other procedural delay tactics to prevent taxpayers from receiving a remedy. A prompt review of the present case would prevent states from experiencing fiscal problems that arise when states are permitted to continue plainly unconstitutional taxation over a long period of time.

CONCLUSION

For the reasons stated above, *amici curiae* respectfully request the United States Supreme Court to accept this case for review.

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In The Supreme Court of the United States

McLANE WESTERN, INC.,

Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF COLORADO, ET AL.,

Respondents.

On Petition For A Writ Of Certiorari To The Colorado Court Of Appeals Division IV

BRIEF OF *AMICUS CURIAE* INSTITUTE FOR PROFESSIONALS IN TAXATION IN SUPPORT OF PETITIONER

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BRIEF OF INSTITUTE FOR PROFESSIONALS IN TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER[1]

This brief is submitted by the Institute for Professionals in Taxation (the "Institute") as *amicus curiae* in support of the Petition for a Writ of Certiorari filed by Petitioner, McLane Western, Inc., dated April 7, 2006, seeking review of the Colorado Court of Appeals' opinion in *McLane Western, Inc. v. Department of Revenue*, 126 P.3d 211 (Colo.Ct.App. 2005), *cert. denied*, 2006 WL 349738 (Colo. Jan. 9, 2006).

I. STATEMENT OF INTEREST OF *AMICUS CURIAE*

The Institute for Professionals in Taxation (or as it is sometimes known, IPT) is an Internal Revenue Code § 501(c)(3) non-profit educational association with members representing corporations, firms, or taxpayers throughout the United States and Canada. It educates, certifies and establishes strict codes of conduct for property, income, and sales and use tax professionals who represent taxpayers. The Institute provides educational opportunities for its members tailored to their professional needs. Professional designation programs in property, income and sales tax leading to the CMI designation

[1] Petitioner, McLane Western, Inc., and Respondent, Colorado Department of Revenue, have consented to the filing of this brief, and their letters of consent have been filed with the Clerk of the Court.

No counsel for a party authored this brief in whole or in part, and no person or entity other than *amicus curiae*, its members, or counsel has made a monetary contribution to the preparation or submission of this brief.

(Certified Member of the Institute) are available to members who satisfy the educational, experience and examination requirements. The Institute is dedicated to the uniform and equitable administration of ad valorem, income and sales and use taxes, to minimizing the cost of tax administration and compliance, and to a high degree of professionalism. Members are expected to adhere to a strict Code of Ethics and Standards of Professional Conduct. IPT members represent the spectrum of business and industry sectors of all sizes – from small firms to Fortune 500 companies, and they share a dedication to further professionalism and cooperation within the tax profession. The Institute and its members therefore have a vital and direct financial interest in prohibiting discriminatory state taxes and in a principled construction of the Commerce Clause.

II. SUMMARY OF ARGUMENT

The imposition of the Colorado tobacco excise tax results in a tax being levied on different tax bases, thereby causing some vendors to pay a higher tax on the same product, to the benefit of Colorado distributors and manufacturers, and to the detriment of out-of-state competitors. The Court should grant certiorari to consider whether the Colorado excise tax, and any other like it that may be enacted throughout the country, contravenes years of Commerce Clause jurisprudence.

III. ARGUMENT

The constitutional analysis adopted by the Colorado Court of Appeals in upholding the Colorado tobacco excise tax as applied to Petitioner, McLane Western, Inc., is

incorrect and inconsistent with the Court's prior interpretation of the Commerce Clause. The Colorado Court of Appeals impermissibly permits the excise tax to be imposed on a different ("shifting") tax base, where that tax base differs depending on whether the distributor or seller of tobacco products is located in Colorado or outside the state.

The decision below creates a competitive disadvantage in the marketplace that is contrary to the Commerce Clause doctrine barring discrimination against products and activities crossing state lines. The Colorado Court of Appeals incorrectly interpreted the Court's Commerce Clause cases by limiting the impact of the Commerce Clause to tax statutes that involve either a difference in tax rates or an exemption from taxation, while permitting a statute that imposes taxes on different tax bases.

If the decision below is allowed to stand, it will provide a broad loophole for states to discriminate against interstate commerce and to evade constitutional challenge by the mere expedient of changing the wording in the state tax statute to eliminate differential tax rates or exemptions. The Colorado Court of Appeals' interpretation of the Court's prior cases is incorrect and results in improper and unconstitutional tax policy that warrants the Court's review.

A. The Colorado Court of Appeals Decision Upholding the Colorado Tobacco Excise Tax Violates the Commerce Clause Because The Colorado Statute Imposes a Different Tax Base on Taxpayers When the Economic Activity Occurs Outside Colorado.

Petitioner McLane Western, Inc. buys tobacco products other than cigarettes, also known as Other Tobacco

Products ("OTP"), from United States Smokeless Tobacco Products, Inc. ("Sales"). Petitioner is located in Colorado. Sales in turn purchases the OTP from United States Smokeless Tobacco Manufacturing, L.P. ("Manufacturing"). Both Sales and Manufacturing are located outside Colorado. Colorado imposes an excise tax on OTP distributed in the state. Colo. Rev. Stat. § 39-28.5-102(1). *See* Petition, App. E at p. 28a. The OTP excise tax of 20% is imposed by Colorado on the first Colorado distributor (essentially upon receipt of the product by that distributor, which here is the invoice price paid by Petitioner to Sales). Because the sales price charged in each segment of the distribution claim is increased ("marked up") to reflect additional marketing costs and profits incurred by the out-of-state companies, the ultimate purchase price paid by Petitioner to Sales for OTP products sold in Colorado is a higher price than if the same products were purchased from a Colorado-based distributor. 126 P.3d at 214.

The disparate economic impact of the Colorado statute can be summarized as follows: when the manufacturer, distributor and seller are located outside Colorado, the tax base and resulting tax burden created by the Colorado statute will be higher than where even one of those entities is located in Colorado. In the instance where the entities are located in Colorado, the excise tax is imposed on the lower price paid by the first Colorado distributor before the price has been marked up.

The imposition of the Colorado OTP excise tax on Petitioner's purchase of OTP violates the third prong of the *Complete Auto Transit* test because it unduly burdens interstate commerce, is discriminatory, and is in violation of the Commerce Clause. *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). The Colorado OTP excise tax

imposes a greater tax burden on Colorado sellers who purchase from out-of-state distributors than those who purchase from in-state distributors.

The Colorado Court of Appeals acknowledged this difference in the tax base and tax burden, before erroneously concluding that because the Colorado tax statute reflects a mere difference in the tax base (what it called the "shifting tax base"), the Colorado tax statute is not facially discriminatory, nor does the statute discriminate against out-of-state competitors in violation of the Commerce Clause. 126 P.3d at 216. The Colorado Court of Appeals determined that cases interpreting the Commerce Clause require there to be a difference in either tax rates or exemptions before there can be any discriminatory impact. 126 P.3d at 214. But the Commerce Clause cases on which it relied do not support that conclusion. The Commerce Clause instead clearly prohibits a state statute like the Colorado OTP excise tax that requires a higher and discriminatory tax base to be imposed on products produced in part, or distributed in part, outside the State. The Court should grant certiorari to consider whether a state tax statute violates the Commerce Clause regardless of whether the discrimination factor is found in the tax rate, in exemptions from the tax, or in the tax base on which the tax is calculated.

The Colorado OTP excise tax violates the Commerce Clause for the same reasons set forth in *Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963), where the Court held that a Louisiana sales tax imposed on oil drilling equipment is unconstitutional where it included a different and discriminatory tax base for equipment purchased from another state. The Louisiana statute did not employ a different tax rate or tax exemption, but

employed a discriminatory tax base that had the same economic result as the Colorado OTP excise tax does here. The Court stated in *Halliburton*, 373 U.S. at 70:

> The inequality of the Louisiana tax burden between in-state and out-of-state manufacturer-users is admitted. Although the rate is the same, the appellant's tax base is increased though the inclusion of its product's labor and shop overhead.

The discriminatory effect of the Colorado OTP excise tax parallels that caused by the state regulation recently criticized by the Court in *Granholm v. Heald*, 544 U.S. 460 (2005). In striking down a state regulatory system that imposed greater restraints on out-of-state than in-state wine distributors, the Court stated unequivocally that "in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter." 544 U.S. at 472 (quoting *Oregon Waste Sys., Inc. v. Department of Environmental Quality*, 511 U.S. 93, 99 (1994)).

The Court similarly recognized in *Granholm* that the proscribed discrimination arises whenever certain vendors are required by the tax system to pay higher fees, costs or taxes, or are subjected to greater licensing or regulatory requirements, 544 U.S. at 474:

> The differential treatment requires all out-of-state wine [distributors], but not all in-state wine [distributors], to pass through an in-state wholesaler and retailer before reaching consumers. These two extra layers of overhead increase the cost of out-of-state wines to Michigan consumers.

The Court has consistently ruled that taxes must be imposed on in-state and out-of-state taxpayers in a non-discriminatory and substantially equivalent manner. As it stated in *Associated Industries of Missouri v. Lohman*, 511 U.S. 641 (1994):

> To ensure that the State is indeed merely imposing countervailing burdens on comparable transactions, we have required that the taxes on interstate and intrastate commerce be imposed on "substantially equivalent event[s]."

Id. at 647 (quoting *Maryland v. Louisiana*, 451 U.S. 725, 759 (1981)).

The Court should grant certiorari to consider whether the Colorado Court of Appeals properly applied this precedent when it held, 126 P.3d at 216:

> The fact that the tax base calculated on the price paid by the taxable distributor may place the product at a competitive disadvantage in the market place because the higher tax is added to the price does not, in our view, render the tax unconstitutional under the Commerce Clause.

Although the Court of Appeals acknowledged the competitive disadvantage placed on distributors purchasing products from out of state, its decision ignores the practical operation of the Colorado OTP excise tax, which unquestionably favors a distributor purchasing from within Colorado over a distributor purchasing from outside Colorado. The Court has repeatedly stressed that under the Commerce Clause a state may not discriminate, no matter what form the discrimination takes, and no matter the mechanics of the statutory scheme that produce the discrimination. The Court has instead flatly

stated that "actual discrimination, wherever it is found, is impermissible." *Associated Industries of Missouri*, 511 U.S. at 650.

The Court emphasized the fundamental fact that the Commerce Clause forbids discrimination, regardless of the form it takes, in *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186 (1994):

> Our Commerce Clause jurisprudence is not so rigid as to be controlled by the form by which a State erects barriers to commerce. Rather our cases have eschewed formalism for a sensitive, case by case analysis of purposes and effects. As the Court declared over 50 years ago: "The Commerce Clause forbids discrimination, whether forthright or ingenious. In each case it is our duty to determine whether the statute under attack, whatever its name may be, will in its practical operation work discrimination against interstate commerce."

Id. at 201 (quoting *Best & Co. v. Maxwell*, 311 U.S. 454, 455-456 (1940)).

The plain fact that a taxpayer purchasing from an out-of-state supplier pays a higher tax has a direct effect on the taxpayer's sales price and profit margin. This tax effect clearly gives the taxpayer who purchases products from in-state suppliers the ability to charge a lower price or increase its profit margin. The Court has repeatedly held that this type of competitive advantage is contrary to the fundamental principles of the Commerce Clause and the Court's own decisions. *See Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 329 (1977) ("No state, consistent with the Commerce Clause, 'may impose a tax which discriminates against interstate commerce . . . by

providing a direct commercial advantage to local business.'" (quoting *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 457 (1959)).

Whether intentional or unintentional, Colorado has created a clear preference for purchasers of in-state products. The Court has stressed that "[T]he prohibition against discriminatory treatment of interstate commerce follows inexorably from the basic purpose of the Clause. Permitting the individual States to enact laws that favor local enterprises at the expense of out-of-state business would invite a multiplication of preferential trade areas destructive of the free trade which the Clause protects." *Boston Stock Exchange*, 429 U.S. at 329. The purchaser of out-of-state products cannot operate on a fair playing field if it is paying a higher *tax*, even though the tax *rate* may be the same. Certiorari should therefore be granted.

B. The Colorado Court of Appeals Decision Upholding the Colorado Tobacco Excise Tax Would Allow Other States to Impose Discriminatory Taxes on Taxpayers When the Economic Activity Takes Place Outside the Taxing State.

The Court of Appeals' decision, if allowed to stand in its present form, would enable a state to draft or redraft a tax statute to withstand constitutional challenge merely by changing its wording to eliminate differential tax rates or exemptions, even while purposely discriminating between taxpayers based solely on the applicable tax base. Not only would this contravene *Halliburton*, and permit states to do an end run around existing Commerce Clause jurisprudence, but it would be poor tax policy.

The decision below threatens to resurrect the very sort of tax statute expressly struck down by the Court in *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984). The West Virginia gross receipts tax struck down in *Armco* imposed a tax on wholesale operations, but exempted in-state manufacturers. Under the Colorado Court of Appeals' reasoning, however, similar statutes could now be enacted to eliminate the tax exemption for in-state manufacturers, instead imposing it on both wholesaling and manufacturing and making it applicable to the first taxable event in the state. The economic result would be similar to the result in Colorado – it would permit what the Colorado Court of Appeals called the "shifting tax base" and thereby discriminate against out-of-state manufacturers and distributors. The same result condemned in *Haliburton* would become constitutionally permissible, at least in the view of the Colorado appellate court. The Court should grant certiorari to address this anomalous result.

IV. CONCLUSION

The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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No. 05-1294

IN THE

Supreme Court of the United States

McLANE WESTERN, INC.,
Petitioner,

v.

DEPARTMENT OF REVENUE, STATE OF COLORADO;
and M. MICHAEL COOKE and FRED FISHER,
as Executive Directors of the Department of Revenue
of the State of Colorado,
Respondents.

On Petition for a Writ of Certiorari to the Colorado Court of Appeals, Division IV

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

QUESTION PRESENTED

Does a state tax on activities related to the distribution of a product in the State, which increases because more stages in the distribution chain are located outside the State rather than within the State, impermissibly discriminate against interstate commerce.

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INTERESTS OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a non-profit public interest law and policy center with supporters in all 50 states.[1] WLF devotes a substantial portion of its resources to defending free-enterprise, individual rights, and a limited and

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[1] Pursuant to Supreme Court Rule 37.6, WLF states that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than WLF and its counsel, contributed monetarily to the preparation and submission of this brief.

accountable government. To that end, WLF has frequently appeared as *amicus curiae* in this and other federal courts to address the proper scope of the Commerce Clause and to challenge State and local legislation that facially discriminates against interstate and/or foreign commerce. *See, e.g., Assoc. Industries of Missouri v. Lohman,* 511 U.S. 641 (1994); *Kraft General Foods, Inc. v. Iowa Dep't of Revenue and Finance,* 505 U.S. 71 (1993).

WLF strongly believes that the economic well-being of this country depends on the unrestricted flow of commerce, both interstate and across our nation's borders. WLF is concerned that a discriminatory taxing scheme such as the Colorado excise tax at issue here will encourage other States and local taxing jurisdictions to adopt similar taxing measures that discriminate against and restrict the flow of interstate commerce.

WLF has no direct financial interest in the outcome of this case. It is filing due solely to its interest in ensuring that the tax laws are not permitted to discriminate against interstate commerce. WLF is filing this brief with the consent of all parties. The written consents have been lodged with the Clerk of the Court.

STATEMENT OF THE CASE

This case is a challenge to the constitutionality of a Colorado excise tax on the distribution of tobacco products in the State. Petitioner McLane Western, Inc. obtains tobacco products from outside of Colorado relatively late in the distribution chain and distributes them to small Colorado retailers. It is uncontested that Colorado imposes a higher excise tax on McLane than it would on another distributor whose products entered Colorado earlier in the distribution

chain. The question presented is whether this differential taxing scheme constitutes facial discrimination against interstate commerce and thus violates the Commerce Clause.

The Colorado courts granted summary judgment against McLane's challenge. Accordingly, for purposes of this petition, McLane's evidence regarding all material facts should be accepted as true – albeit WLF does not understand that Respondents seriously contest any of that evidence. Rather, the parties' disagreements focus on the legal conclusions to be drawn from the largely uncontested facts.

WLF adopts the Statement of the Case set forth in the Petition. WLF wishes to highlight several additional factual issues, in light of the "Counterstatement of the Facts" set forth in Respondents' opposition brief. First, Respondents make repeated reference to the corporate relationship between the company that manufactures the tobacco products at issue in this case (United States Tobacco Manufacturing Company, Inc. or "UST Manufacturing") and the company that serves as the initial distributor for those products (United States Tobacco Sales and Marketing Company, Inc. or "UST Sales"). Respondents note that UST Manufacturing and UST Sales are subsidiaries of the same parent corporation (U.S. Smokeless Tobacco Co. or "US Smokeless"). Opp. Br. 1. But while Respondents mention that fact repeatedly, evidently in hopes that doing so will somehow diminish McLane's claims, nowhere do Respondents suggest that the transactions between the corporations are anything other than arms-length or otherwise explain how they think the corporate relationship between UST Manufacturing and UST Sales affects the Commerce Clause analysis.

Indeed, the Colorado Court of Appeals made clear that the issue of the relationship between UST Manufacturing and

UST sales had not been raised by the parties and consequently played no role in its decision. Petition Appendix ("Pet. App.") 3a. Accordingly, the Commerce Clause rule established by the courts below applies broadly to all distribution chains, not simply to those involving two or more affiliated corporations; and thus the cert-worthiness of this case is unaffected by the fact that two (non-party) corporations involved in the distribution chain are related.

Second, WLF concurs with Respondents' assessment that "many other states" impose an excise tax on tobacco products in a manner "similar" to Colorado.[2] In WLF's view, the widespread adoption of such excise tax schemes highlights the importance of the issues raised by the Petition.

Third, Respondents state that Colorado wrote its OTP excise tax statute as it did "to ensure that companies cannot avoid their obligation to pay the tax simply by reorganizing into separate manufacturing and supply subsidiaries" and thereby "to achieve the same result no matter what the structure of the manufacturing and supply system from which a distributor purchases OTP." Opp. Br. 3. Respondents supply no citations to support their claim regarding statutory intent, and WLF is aware of nothing in the record that provides such support. Moreover, Respondents' explication of the excise tax statutes is inconsistent with the court of appeals's definitive interpretation. Contrary to Respondents' assertion, the appeals court held that the excise tax would, indeed, be reduced if a distributor purchases OTP from an in-state source,

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[2] The excise tax at issue here imposes a tax on "the sale, use, consumption, handling, or distribution" in Colorado of certain tobacco products – in general, all tobacco products other than cigarettes. Colo. Rev. Stat. § 39-28.5-102. These products are often referred to as "other tobacco products" or "OTP."

and it gave no indication that its analysis would be affected if the in-state source were in some way related to the manufacturer. Pet. App. 6a.

Proceedings Below. McLane filed suit in a Colorado district court, seeking a refund of in excess of $10 million in OTP excise taxes paid between 1991 and 2002. McLane claimed, *inter alia*, that the excise tax violated the Commerce Clause because the tax was approximately twice as high as it would have been had the OTP either been manufactured in Colorado or had entered Colorado at an earlier stage of the distribution process. The district court rejected the Commerce Clause claim and granted summary judgment to Respondents. Pet. App. 14a-24a.

The court of appeals affirmed, finding that the Colorado excise tax on OTP did not violate the Commerce Clause. *Id.* 1a-13a. Rejecting the interpretation of the tax statute espoused by Respondents in this Court, the appeals court agreed with McLane that a distributor's "tax base" – and thus the distributor's total tax bill – "will be higher the later in the distribution network the product is taxed" and that "the location [*i.e.*, either in-state or out-of-state] of the manufacturers, suppliers, or distributors involved in the product's distribution network and the price mark-up of each impacts the tax base or the price upon which the constant twenty percent tax rate is imposed." *Id.* 6a.

The appeals court nonetheless listed several reasons why it did not believe that the excise tax discriminated against interstate commerce in violation of the Commerce Clause. First, the court said that § 39-28.5-102's shifting tax base would not encourage out-of-state manufacturers or distributors (such as UST Manufacturing or UST Sales) to move into Colorado because they "might well" themselves become

subject to the OTP excise tax. *Id.* 7a. Second, the court said that the tax does not discriminate because it is "imposed on an activity within the state, the sale and distribution of OTP, not on the product or the distribution network." *Id.* The court reasoned that the tax could not be deemed discriminatory simply because some distributors may be placed at a competitive disadvantage by being forced to pay a higher tax based on the greater value of the late-in-the-distribution-chain product they purchased, because "[a]ll taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion." *Id.*

Third, the court said that distributors are treated the same regardless whether they are residents of Colorado: "Out-of-state manufacturers or distributors may engage in commerce within Colorado without suffering any burden from which local distributors or manufacturers are exempted." *Id.* 10a. The appeals court made no attempt to explain how that observation was applicable to McLane's Commerce Clause claim. McLane, after all, is an in-state firm headquartered in Colorado; and its suit is based not on a claim that it is suffering burdens not imposed on similarly situated competitors, but on a claim that it is bearing an increased tax burden solely because its OTP arrives in Colorado relatively late in the distribution chain.

The Colorado Supreme Court denied a petition for review on January 9, 2006. *Id.* 26a-27a.

REASONS FOR GRANTING THE PETITION

This case presents issues of exceptional importance, both to the many businesses enterprises whose tax assessments are based at least in part on the interstate nature of their business activities, and to State and local officials who seek to ensure

that their tax systems impose a fair share of the tax burden on such enterprises without running afoul of the Commerce Clause. While the Court has invoked the "dormant Commerce Clause" to restrict taxation of interstate commerce in a wide variety of situations, at its heart that clause is designed to prevent taxation that facially discriminates against interstate commerce. Yet, as this case well illustrates, there is widespread confusion in the state courts regarding just what constitutes "facial discrimination." Indeed, the fact that the Colorado courts, as well as courts from a number of other states, could fail to recognize the transparently discriminatory features of the excise tax scheme being challenged here, underscores the extent of the confusion regarding when a tax scheme should be condemned as facially discriminatory. Review is warranted to provide guidance that could go a long way in clearing up the confusion.

The Court has often spoken of the need for bright-line rules in this area of constitutional law, to reduce litigation and to permit businesses and taxing authorities to engage in long-term planning with a clearer understanding of their rights and responsibilities under the Commerce Clause. The bright-line rule sought in this case – that increased tax burdens imposed on interstate commerce are just as discriminatory when imposed through use of increased tax bases as they are when imposed through use of increased tax rates – is fully supported by the Court's dormant Commerce Clause decisions and would provide an easy-to-apply rule that should reduce litigation significantly. Moreover, the proposed bright-line rule would not impair the ability of State and local governments to raise revenues; they have available to them numerous alternative tax structures that avoid discrimination against interstate commerce yet would be likely to raise revenues comparable to those raised by the challenged scheme.

This Petition provides a particularly good vehicle for addressing the issue of what constitutes facial discrimination against interstate commerce. There is nothing interlocutory about the case; a final judgment has been entered against McLane. Respondents suggest that review is inappropriate because the case presents "an insufficient record and a unique factual situation." Opp. Br. 13. To the contrary, the record is as complete as it is likely ever to be: WLF is unaware of any material factual disputes between the parties, and Respondents do not suggest any. Both parties moved in the trial court for summary judgment with the understanding that there were no disputed issues of material fact and that they disagreed only about the applicable law. Moreover, the Colorado courts have established a rule that is broadly applicable to all distribution chains, not simply to business entities whose situation is identical to McLane's. Furthermore, Respondents have conceded that their excise tax scheme is not "unique" but rather is similar to tax schemes adopted by "many other states." *Id.* at 3. Under those circumstances, there is no good reason to defer resolution of the clear legal issues raised by this Petition.

I. REVIEW IS WARRANTED TO CLEAR UP WIDESPREAD CONFUSION REGARDING WHAT CONSTITUTES "FACIAL DISCRIMINATION" AGAINST INTERSTATE COMMERCE

The Constitution's Commerce Clause (Art. I, § 8, cl. 3) grants Congress the broad authority to regulate interstate commerce, including the power to regulate State taxation of interstate commerce. The Court has long understood the Commerce Clause also to include a "negative" aspect – that is, even in the absence of congressional action, it imposes limitations on State authority to impose regulatory measures that unduly burden interstate commerce for the benefit of in-

state economic interests. *See, e.g., Fulton Corp. v. Faulkner*, 516 U.S. 325, 330 (1996).

The Court has articulated a variety of tests to determine the point at which a burden on interstate commerce becomes constitutionally impermissible, leading to no small degree of confusion in the law. That confusion, as well as the absence of any clear textual support for the "negative" aspect of the Commerce Clause, has led some Justices to suggest that the Court should avoid further expansion of the negative Commerce Clause. *See, e.g., West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 210 (1994) (Scalia, J., concurring in the judgment). Instead, those Justices have advocated focusing enforcement of the negative Commerce Clause primarily on those cases in which State law "facially discriminates against interstate commerce." *Id.* While a majority of the Justices has never endorsed such a formal retrenchment, the Court nonetheless has made absolutely clear that State regulations that facially discriminate against interstate commerce are particularly disfavored under the negative Commerce Clause. Just last term, the Court explained:

> Time and again this Court has held that, in all but the narrowest circumstances, state laws violate the Commerce Clause if they mandate "differential treatment of in-state and out-of-state economic interests that benefits the former and burdens the latter."

Granholm v. Heald, 544 U.S. 460, 472 (2005) (quoting *Oregon Waste Systems, Inc. v. Dep't of Environmental Quality of Oregon*, 511 U.S. 93, 99 (1994)).

One of the supposed virtues of the rule flatly prohibiting "facial discrimination" against interstate commerce is that it is thought to provide a "clear, rational line" between permissible

and impermissible forms of State regulation. *West Lynn Creamery*, 512 U.S. at 212 (Scalia, J., concurring in the judgment). But the rule cannot continue to serve that purpose unless the Court is willing to step forward periodically and provide guidance regarding what constitutes "facial discrimination." The circumstances of this case suggest that such guidance is urgently needed.

By any objective measure, Colorado's excise tax treats the handling of OTP arriving from out-of-state less favorably than it treats the handling of OTP already present in the State. Moreover, that less favorable treatment can only be deemed "facial" in the sense that the fact of less favorable treatment is apparent from the face of the excise tax statute, without any need to rely on information not set forth in the statute. Section 102 makes clear that it is the act of bringing OTP into the State (or the manufacture of OTP within Colorado) that causes the tax to be levied.[3] Section 102 further provides that the tax is to be imposed at a rate of 20% of the "the manufacturer's list price," a term that the Colorado Court of Appeals authoritatively construed to mean the price paid by the distributor for the OTP it receives. Pet. App. 12a-13a. Accordingly, it is apparent from the face of the excise tax statute that a distributor who brings OTP into Colorado at a later stage of the distribution chain (when the price has already been marked up to reflect the distribution, sales, and promotional activities of earlier distributors) will pay a higher excise tax than will a distributor who brings identical OTP into

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[3] Section 39-28.5-101, by defining "the distributer" (upon whom the tax is levied under § 102) as limited to the entity that *first* brings the OTP into Colorado, makes clear that the excise tax may only be applied once on any given shipment of OTP, regardless of how many times it changes hands among distributors within Colorado before reaching a retailer.

Colorado at an earlier stage of the distribution chain. Indeed, as noted above, the court of appeals readily recognized that that is precisely the effect of the excise tax. Pet. App. 6a.

In light of the appeals court's clear understanding of how the statute operated, its failure to deem the statute facially discriminatory against interstate commerce can only be attributed to confusion regarding what constitutes the "facial discrimination" that this Court has so often and so roundly condemned. The extent of that confusion is underscored by the appeals court's citation to decisions from other State courts that have rejected Commerce Clause challenges to similar excise tax schemes. *Id.* 10a-12a (citing *Kansas Tobacco-Candy Distributors & Vendors, Inc. v. McDonald*, 214 Kan. 67, 73 (1974); and *McLane Co. v. Washington State Dep't of Revenue*, 105 Wash. App. 409, 414-15 (2001)).

As the petition more than adequately explains, the decision below was rendered in the face of seemingly clear precedent from this Court condemning State taxation as "facially discriminatory" in closely analogous factual situations. *See Halliburton Oil Well Cementing Co. v. Reily*, 373 U.S. 64 (1963); *Armco, Inc. v. Hardesty* , 467 U.S. 638 (1984). Rather than repeating in full McLane's explanation regarding why the decision below conflicts with those cases, WLF wishes to make a few brief comments. First, both the appeals court and Respondents argue that *Halliburton* is distinguishable because a key factor relied on by the Court in *Halliburton* (the tendency of the state tax to pressure out-of-state entities to move their operations to the taxing state) is not present here. Pet. App. 8a; Opp. Br. 10-11. They assert that UST Sales would never be tempted to open a facility in Colorado because doing so would render it subject to the OTP excise tax. *Id.* That argument makes no sense. As noted above, § 101 bars multiple applications of the excise tax to a

single OTP shipment, even if it changes hands several times within Colorado. Thus, if UST Sales opened a facility in Colorado and the OTP excise tax were imposed on UST Sales, then the tax would not also be imposed on McLane. In that event, UST Sales would pay a far lower excise tax (based on its purchase price from UST Manufacturing) and would include that tax in the price it charged McLane. Even with that increased price, the net cost to McLane (after taking into account its own tax savings) would be considerably less than the current price. Accordingly, the current structure of the excise tax provides UST Sales with a strong incentive to open up a Colorado facility – even though doing so may cause it to forgo cost savings that may well accrue from maintaining a single nationwide distribution facility. *See Halliburton*, 373 U.S. at 72 (the discriminatory Louisiana tax could lead to "fractionalization" of the out-of-state firm's operations, a result "destructive of the very purpose of the Commerce Clause.").

Second, the appeals courts' rationale for deeming the OTP excise tax non-discriminatory conflicts with numerous decisions of this Court. The appeals court reasoned that no discrimination against interstate commerce exists in this case because "[a]ll taxable distributors of OTP are taxed at the same rate and on a tax base determined in the same fashion." Pet. App. 7a. But this Court has determined in numerous cases that a State tax facially discriminated against interstate commerce even though the State's tax *rate* on interstate commerce was identical to or less than the tax rate imposed on comparable in-state activities. *See, e.g., Halliburton*, 373 U.S. at 70 (the fact of identical tax rates is not controlling; "equality for the purposes of competition is measured in dollars and cents, not legal abstractions"); *South Central Bell Telephone Co. v. Alabama*, 526 U.S. 160, 169 (1999) (corporate franchise tax discriminated against out-of-state corporations, even though tax rate imposed on out-of-state corporations was less than 1/3

the franchise tax rate imposed on domestic corporations). Moreover, the appeals court's statement that a tax qualifies as nondiscriminatory simply because the tax base is determined in the same fashion for all businesses cuts against this Court's entire line of tax discrimination cases. Challenged taxes virtually always treat all businesses in accordance with a uniform set of rules and permit *any* business to reduce the tax burden by altering its business operations (such as by moving some of its operations in-state). But the ability of businesses to avoid discriminatory taxation in that manner has never been deemed sufficient to avoid application of the dormant Commerce Clause.

In sum, the decision below, as well as other state court decisions relied on by the court of appeals, sharply conflict with decisions of this Court that prohibit State taxes that facially discriminate against interstate commerce, and suggest widespread confusion regarding what constitutes facial discrimination. Review is warranted to clear up that confusion.

II. REVIEW IS WARRANTED BECAUSE ESTABLISHMENT OF BRIGHT-LINE RULES REGARDING FACIAL DISCRIMINATION PROMOTES STABILITY AND REDUCES LITIGATION

Quite apart from the need to clear up widespread confusion regarding what constitutes "facial discrimination," review is warranted because the establishment of bright-line rules of the sort requested by McLane serve important societal interests. The petition requests the Court to address – and to create a bright-line rule regarding – whether State taxes that have the effect of imposing a differential tax burden on interstate commerce by increasing the tax base of that

commerce in comparison to the tax base of in-state activities, should be deemed facially discriminatory. Establishing a bright-line rule on that issue, which (as McLane demonstrates) has arisen in many different states, would reduce litigation in this area and provide stability in the law, and thereby would permit both States and businesses to engage in long-term planning with a clearer understanding of their rights and responsibilities under the Commerce Clause.

The Court recently addressed the value of bright-line Commerce Clause rules, in a slightly different but closely related context. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), addressed the issue of whether a "substantial nexus" existed between the taxing State and the activity to which the tax was to be applied.[4] The Court recognized that drawing a line between cases in which the nexus is sufficiently substantial and those in which it is not can be a somewhat arbitrary exercise. Nonetheless, the Court also recognized that drawing a clear line *somewhere* has substantial virtue because doing so reduces litigation and permits parties to engage in long-term planning in reliance on a clear rule. Accordingly, the Court affirmed a bright-line rule that it had established 25 years earlier in *National Bellas Hess, Inc. v. Dep't of Revenue of Illinois*, 386 U.S. 753 (1967) – that a State may not impose a duty to collect use taxes on a seller if the seller's only connection with customers in the taxing State is by common carrier or the U.S. mail – even though it recognized that the *National Bellas Hess* rule was somewhat arbitrary and based on outmoded, "formalistic" notions regarding the scope of the

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[4] The "substantial nexus" test is one of the four tests that a challenged State tax must pass in order to survive a negative Commerce Clause challenge. *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). Another one of the four *Complete Auto* requirements is that the tax not discriminate against interstate commerce. *Id.*

Commerce Clause. *Quill*, 504 U.S. at 314-16. The Court determined that *National Bellas Hess*'s bright line rule "further[ed] the ends of the dormant Commerce Clause," *id.* at 314, explaining:

> Like other bright-line tests, the *Bellas Hess* rule appears artificial at its edges. . . . This artificiality, however, is more than offset by the benefits of a clear rule. Such a rule firmly establishes the boundaries of legitimate state authority to impose a duty to collect sales and use taxes and reduces litigation concerning these taxes. This benefit is important, for as we have so frequently noted, our law in this area is something of a "quagmire," and the "application of constitutional principles to specific state statutes leaves much room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation." *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 457-458 (1959). Moreover, a bright-line rule in the area of sales and use taxes also encourages settled expectations and, in doing so, fosters investment by businesses and individuals.

Quill, 504 U.S. at 315-16.

Similarly, the bright-line rule requested by McLane would decrease litigation and encourage settled expectations. Colorado contends that taxing schemes that can (as the court of appeals recognized in this case) lead to increased tax burdens on interstate commerce should not be deemed facially discriminatory when they arise due merely to unequal tax bases and not uneven tax rates. It is theoretically possible that in some case a State could demonstrate that uneven tax bases that favor in-state entities should nonetheless be deemed not to constitute facial discrimination against interstate commerce.

But to allow case-by-case adjudication of that issue would encourage increased litigation and prevent the creation of settled expectations in the area. Review is warranted to determine whether States and businesses would be better served by creating a bright-line rule that unequal tax bases are to be treated the same as unequal tax rates in determining whether a State tax facially discriminates against interstate commerce.

Moreover, the proposed bright-line rule would not impair the ability of State and local governments to raise revenues; they have available to them numerous alternative tax structures that avoid discrimination against interstate commerce yet would be likely to raise revenues comparable to those raised by the challenged scheme. For example, Colorado could adopt a statute that imposes the OTP excise tax on the final distributor that provides the product directly to the retailer, and bases its tax on the amount paid by the final distributor for the product. Such a scheme would raise at least as much revenue as the current excise tax, yet would ensure that all distribution chains would be taxed the same – without regard to the percentage of the distribution process that takes place in Colorado.

III. THIS CASE PROVIDES A PARTICULARLY GOOD VEHICLE FOR ADDRESSING THE ISSUE RAISED BY THE PETITION

Review is warranted for the additional reason that the case provides a particularly good vehicle for addressing the issue raised by the petition.

First, there is nothing interlocutory about the petition. A final judgment has been entered against McLane, so denial of the petition will not result in further development of the record.

Respondents suggest that review is inappropriate because the case presents "an insufficient record and a unique factual situation." Opp. Br. 13. That contention is without merit. The record here is as complete as it is ever going to be in a case of this sort. Respondents have not suggested any types of evidence, absent from the record in this case, that would facilitate the Court's consideration of the discriminatory effects of shifting tax bases. WLF is unaware of any material factual disputes between the parties, and Respondents do not suggest any. Both parties moved in the trial court for summary judgment with the understanding that there were no disputed issues of material fact and that they disagreed only about the applicable law. Under those circumstances, there is no reason to defer consideration of the issue presented in hopes of finding a case with a complete trial record raising the same issue.

Nor is there any reason to conclude that this case presents a "unique factual situation." The Colorado courts in this case have established a rule that is broadly applicable to all distribution chains, not simply to business entities whose situation is identical to McLane's. They have determined that the Commerce Clause does not limit the power of a State to impose a greater tax burden on distribution chains that entail bringing a product into the State at the tail end of the distribution chain, than on distribution chains that entail bringing an identical product into the State earlier in the distribution chain. That rule is broadly applicable to large number of firms doing business in Colorado.

Furthermore, Respondents have conceded that their excise tax scheme is not "unique" but rather is similar to tax schemes adopted by "many other states." *Id.* at 3. Given the broad-based applicability of the issue raised by the petition, review by this Court is fully warranted.

Nor does the fact that UST Manufacturing and UST Sales are related entities counsel against granting review. As noted above, the Colorado Court of Appeals made clear that the issue of the relationship between UST Manufacturing and UST sales had not been raised by the parties and consequently played no role in its decision. Pet. App. 3a. Accordingly, the Commerce Clause rule established by the courts below applies broadly to all distribution chains, not simply to those involving two or more affiliated corporations; and thus the cert-worthiness of this case is unaffected by the fact that two (non-party) corporations involved in the distribution chain are related. Indeed, while Respondents' opposition brief repeatedly mentions that UST Manufacturing and UST Sales are related entities, evidently in hopes that doing so will somehow diminish McLane's claims, nowhere do Respondents suggest that the transactions between the corporations are anything other than arms-length or otherwise explain how they think the corporate relationship between UST Manufacturing and UST Sales affects the Commerce Clause analysis.

Moreover, as noted above, the excise tax scheme creates pressure on UST Sales to establish facilities in Colorado, and nowhere do Respondents present any argument suggesting that the relationship between UST Manufacturing and UST Sales should prevent those involved in the OTP distribution chain from relying on such a move of facilities as a basis for slashing excise tax payments by the OTP distribution chain.

In sum, should the Court determine that it wishes to take up the issue presented by the petition, this case provides an excellent vehicle for doing so.

CONCLUSION

Amicus curiae Washington Legal Foundation respectfully requests that the Court grant the petition for a writ of certiorari.

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